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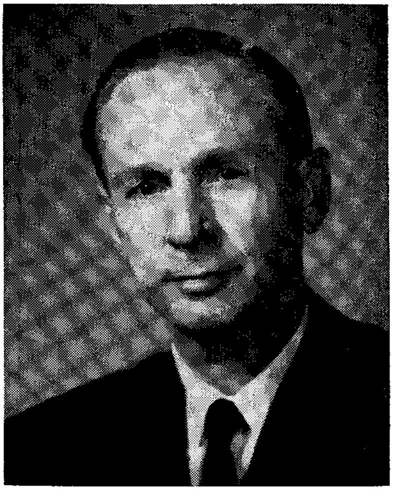

David J. Clarke received his LL.B. degree at the University of Montana in 1938. He was admitted to practice in Colorado in 1946. Prior to entering private practice in Denver in 1953, he served as attorney with the Anti-trust Division of the U. S. Department of Justice, with the U. S. Atomic Energy Commission, and with the Wage Stabilization Board. He was elected to the Colorado House of Representatives in 1954 and is now serving his first term in the State Senate. Mr. Clarke is a member of the Colorado and Denver Bar Associations.

THE NEW COLORADO CORPORATION ACT

BY DAVID J. CLARKE

INTRODUCTION[1]

The new Colorado Corporation Act becomes effective January 1, 1959. It is based upon the 1953 revision of the Model Business Corporation Act prepared by the Committee on Corporate Laws of the American Bar Association. The following extracts from the preface to the 1950 revision of the Model Act explain its background and some of the criteria and purposes of its originators.[2]

> "The primary purpose of the Model Act is to provide state commissions and bar association committees with a working model for revision and modernization of their corporate laws. . . . It represents the collective experience and sound views of a widely diversified group of lawyers active in corporate practice, and is offered as a public service in the field of business corporation law.

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[1] Explanation of footnote citations: Any chapter, article and section citation from § 31-1-1 through § 31-26-8 refers to the law as codified prior to January 1, 1959, and any chapter, article and section citation from § 31-27-1 through § 31-36-12 refers to sections of the Colorado Corporation Act (Colo. Laws 1st Reg. Sess. 1958, c.32) which becomes effective January 1, 1959, as such Act will be codified according to the present plans of the Revisor of Statutes. There is set forth on page 366 a table of: (1) comparable prospective sections of the 1959 supplement to Colo. Rev. Stat. (1953), (2) the sections of Ch. 32 of the 1958 Colorado Session Laws, and (3) the sections of the Model Act (Revised 1953). Where revisions proposed by the A.B.A. Committee in 1955 and 1957 were included in the Colorado Corporation Act, references are made to the pamphlets issued by the Committee during those years. The section numbers of Ch. 32 of the 1958 Session Laws are set forth in brackets after the prospective code section numbers. Until publication of the 1959 Supplement to Colo. Rev. Stat. (1953), only the section numbers in brackets are usable.

[2] Preface, Model Bus. Corp. Act (rev. 1953).

"No attempt has been made to abandon all present day laws and practices in favor of revolutionary ideas. On the contrary the Committee has preserved and codified those that are sound in principle. Some of the ideas still found in many state laws have been incorporated because they lead to better understanding and administration, but on the whole the Model Act presents a well organized code of the best in existing statutes without substituting entirely new concepts of corporate law.

"A great deal of consideration has been given to the rights of shareholders. . . . The Committee believes that the rights of shareholders should be strengthened, not weakened, and should be clearly defined.

"Another attractive feature of the Model Act is its flexibility. Many provisions for the regulation of internal affairs of a corporation may be inserted in its articles of incorporation or in its by-laws, as desired. Flexibility is obtained in the option to include or omit such matters, but in the interest of certainty, where the articles and by-laws are silent, the rules are stated in the act.

"The Committee presents the Model Act as a modern statute that preserves in proper balance the interests of the state and the rights and interests of corporations, shareholders and management. It may not appeal to a state that is soliciting corporate business, but it will be attractive to any state that seeks to provide a sound and modern law under which its business corporations in general can be organized and continue to exist. Uniformity of corporation laws among the states would be of inestimable value to business and our profession. The Committee believes that its Model Act is worthy of uniform adoption."

The Corporation, Banking and Business Law Committee of the Colorado Bar Association, under the chairmanship of Robert S. Gast, Jr., studied each section of the Model Act during meetings held in 1956 and recommended to the 1957 General Assembly the adoption of a bill based on the Model Act. That bill became House Bill No. 150. It passed the House of Representatives, but failed to pass the Senate. However, the Senate Judiciary Committee recognized that the bill deserved careful consideration, and an interim committee of three Senate Judiciary Committee members was appointed to study the bill during 1957 and report its recommendations to the full Committee during the 1958 General Assembly.

The interim committee, consisting of Senators Ranger Rogers, Roy H. McVicker, and this author, was fortunate to obtain the assistance and advice of Homer H. Clark, Professor of Law at the University of Colorado. Several meetings were held during 1957 with the Corporation Committee of the Colorado Bar Association. After full discussion of House Bill No. 150, the interim committee and the Corporation Committee agreed upon a substantial number of revisions, and a revised proposal—Senate Bill No. 14—was introduced in January 1958. Since the proposal was introduced during the limited, special session, special efforts were made to iron out all controversial provisions prior to introduction.

Throughout this article liberal use has been made of memoranda of members of the Colorado Bar Association Corporation Committee, memoranda of Professor Clark to the interim committee, and the comments contained in the Model Act. These memoranda help to explain the new Colorado Corporation Act.

The Colorado Corporation Act is, then, the product of years of work by members of the Corporation, Banking, and Business Law Committees of the American and Colorado Bar Associations. The Model Act has been used as a basic form for other jurisdictions which have modernized their corporation laws. Those jurisdictions include Alaska,[3] District of Columbia,[4] North Dakota,[5] Oregon,[6] Texas,[7] Virginia,[8] and Wisconsin.[9] Similar revisions are under consideration in Arizona, Iowa, South Dakota, Utah, and a number of other states.[10]

The legislative interim committee was advised of criticisms of the Model Act contained in several law review articles.[11]

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[3] Alaska Sess. Laws, 1957, c.168.
[4] D.C. Code Ann. § 29.901-956 (Supp. 1955).
[5] N.D. Sess. Laws. 1957, c.102.
[6] Ore. Rev. Stat. § 57.002-994 (1953).
[7] Tex. Rev. Civ. Stat. Arts. 1302-1538 N (Supp. 1955).
[8] Va. Acts, 1st Reg. Sess. 1956, c.428.
[9] Wis. Stat. § 180.01-.97 (1953).
[10] The A.B.A. Committee on Corporate Laws is annotating each section of the Model Act, and will compare each section with the statutes of the various states, show its history to the extent pertinent, discuss the general case law on the problems covered, and give references to texts and law reviews which will facilitate further study. A sample annotation appears in 13 The Business Lawyer 693 (1958) (this is the official publication of the A.B.A. Section on Corporation, Banking and Business Law).
[11] Luce, Trends in Modern Corporation Legislation, 50 Mich. L. Rev. 1291 (1952) (in which the Wisconsin adaptation of the Model Act is discussed); Ballantine, Questions of Policy in Drafting a Modern Corporation Law, 19 Calif. L. Rev. 465 (1931).

In one such article, an eminent writer on corporation law stated:

> "A serious dilemma in drafting a corporation law is to make it liberal enough to facilitate business transactions without undue formalities of checks and balances, of votes and consents of shareholders, and applications to courts; and at the same time not so lax that the management or the majority may manipulate the machinery to the prejudice of the creditors or investors or the oppression of minority shareholders. The practical difficulty must be always remembered that with the freedom of admission of foreign corporations to do business in the state and the exemption of the internal organization and affairs of such corporations from local regulation, it is perfectly useless to impose drastic limitations and requirements that would simply have the effect of driving corporations from their home state to more hospitable shores."[12]

The legislative interim committee rejected a good many demands for "liberal" (pro-management) revisions of the Model Act which, it was asserted, would have made the new corporation law "competitive" with the most liberal provisions of other states.[13] Other departures were made in order to adhere to existing Colorado Law. The principal objective was to modernize the Colorado law relating to business corporations, using the Model Act as a guide, and at the same time to make as few radical changes as possible. Whether such a laudable objective was achieved depends upon one's point of view as a legislator, a majority or minority shareholder, a creditor, a management executive, a preferred shareholder, a promoter, or an economist.

To the extent shown by the asterisks in the Table of Comparative Section Numbers appearing as an appendix immediately following this article, the Model Act was adopted in Colorado; for the balance of the sections, the Model Act served as a substantial guide.

The legislature recognized that a safeguard of sorts arose from the fact that the effective date of the act is January 1, 1959, and that, if publicity given the act prior to its effective date should raise substantial objections to any provision, a curative amendment can be presented to the 1959 General Assembly.

The Revisor of Statutes has stated that he proposes to codify the Colorado Corporation Act by adding ten new articles to Chapter 31, Colorado Revised Statutes of 1953. Therefore, the new act is analyzed

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12 Ballantine, supra note 11 at 465.

13 Some departures from the Model Act, to which the interim committee acceded, are discussed in Emerson, Vital Weaknesses in the New Virginia Stock Corporation Law and the Model Act, 42 Va. L. Rev. 489 (1956), which did not come to the present writer's attention until this article was commenced.

according to the proposed codification which is shown in the Table of Comparative Section Numbers at the end of this article.

This article is presented to Colorado lawyers and other interested persons from a legislator's point of view with the hope that further improvements in the corporation laws of Colorado will result. An understanding of many sections of the new law will be facilitated if such sections are read when references are made to them in the remainder of this paper.

APPLICATION AND DEFINITIONS

A. APPLICATION

Except as noted below, the Colorado Corporation Act, effective January 1, 1959, apparently will apply to all business corporations in existence on that date or thereafter organized.[14] However, any right, liability or penalty accrued or incurred under prior law is not affected.[15]

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[14] § 31-27-4, [141]. Specifically repealed were all of articles 1, 2, 3, 4, 5, 6, 7, 8, 10 and 19 of Ch. 31, and all of article 2 of Ch. 138, Colo. Rev. Stat. (1953); and all of chapters 89, 90, 91, 92, 93 and 94 (Sess. L. 1955); and all of chapters 101 and 103 (Sess. L. 1957).

[15] § 31-27-6, [144].

The new act will apply to corporations organized under special statutes; but to the extent that the new act is inconsistent with those special statutes, the latter will apply.[16]

Corporations may be organized under the new law for any lawful purposes.[17] However, a statute requiring corporations of a particular class[18] to be organized exclusively thereunder takes precedence over the new law. Furthermore if another statute requires corporations of a particular class to be organized under that other statute and also under general corporation laws, both the special statute and the new act will apply. Where organizers have a choice of incorporating under a special statute or under the new general act, they may elect. If the articles do not disclose the election, the corporation will be considered to have been organized under the new law.[19]

B. DEFINITIONS

The section on definitions,[20] fortunately, follows the Model Act, with only insignificant changes. Only the more important definitions will be discussed here.

The definition of treasury shares[21] in subsection (h) makes it clear that they are to be considered issued but not outstanding shares.[22] Treasury shares reacquired may be cancelled upon acquisition[23] or by corporate action subsequent to acquisition.[24] Unless so cancelled, reacquired shares have the status of treasury shares. Treasury shares are not entitled to vote,[25] and, since they are not "outstanding" shares, are not counted in computing the required vote under the numerous provisions of the act specifying a required vote of shares. Section 5 of the new law[26] restricts the power of a corporation to acquire its issued shares and permits their disposition, and section 17 of the new law[27] permits the directors to fix the consideration for their disposition.

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16 § 31-27-3 (d), [3 (d)].
17 § 31-27-3, [3].
18 Corporations of a particular class are, for example, banks, savings and loan associations, insurance corporations, title and guaranty companies, mining, telegraph, ditch and reservoir, flume and pipeline, toll road, and bridge and ferry companies, water users associations, and non-profit corporations, religious, educational and benevolent societies, joint stock religious or benevolent associations, cooperative associations, agricultural and livestock associations, non-profit cooperatives and cemetery companies.
19 § 31-27-3, [3].
20 § 31-27-2, [2].
21 § 31-27-2 (h), [2 (h)].
22 Professor Clark informed the interim committee: "This clears up, at least to some extent, the status of treasury shares which in Colorado has been somewhat confused due to the Supreme Court's failure to understand their true nature. The case is Colorado Industrial Loan and Investment Company v. Clem, 82 Colo. 399 (1927) in which the Court seems to treat treasury shares as if they were an asset of the corporation, which of course they are not, in the usual sense." Memorandum of Aug. 14, 1957 to the Interim Committee.
23 § 31-32-3, [63].
24 § 31-29-6, [54] or § 31-32-4, [64].
25 § 31-30-16, [32].
26 § 31-28-2.
27 § 31-30-4.

"Net assets" means the amount by which the total assets of a corporation, excluding treasury shares, exceed the total debts. The stated capital, the surplus accounts and surplus reserves, if any, of a corporation are not in any sense a debt. In effect, the term "net assets" is equivalent to the concept of net worth. The term "net assets" is used in section 43 (d) [28] which restricts distribution in partial liquidation, and in section 62[29] which restricts the power of a corporation to redeem or purchase redeemable shares.

"Stated capital" is defined to avoid the ambiguity which has frequently resulted from the use of the terms "capital" and "capital stock." The determination of stated capital is prerequisite to the determination of surplus which is defined to mean the excess of net assets over stated capital.[30] Generally speaking "stated capital" is the aggregate par value of shares with a par value and that part of the consideration received for no par shares not allocated to capital surplus.[31] It may be increased by transfers from surplus as a result of an exchange or conversion of shares,[32] by the declaration and payment of a share dividend out of authorized but unissued shares,[33] or by amendment to the articles of incorporation.[34] It may be decreased by a distribution in partial liquidation,[35] by an amendment to the articles of incorporation,[36] by the redemption and cancellation of redeemable shares,[37] by the cancellation of other reacquired shares,[38] or by consent of the shareholders.[39]

The new act defines and employs a number of terms to clarify the law in regard to dividends and other distributions to shareholders. It employs the accepted legal definition of surplus, dividing all surplus into "earned surplus" and "capital surplus." "Earned surplus"[40] as defined, may be generally described as the accumulated and undistributed net income and profits of a corporation from the time of its organization. "Capital surplus" is all surplus that does not fall within the definition of earned surplus. However, because capital surplus can be applied to reduce or eliminate a deficit if there is no earned surplus,[41] the computation of earned surplus at any time after such an application must have as its starting point the date capital surplus was last so applied. Earned surplus, at any time, includes current profits and is not necessarily a year-end figure.

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28 § 31-31-11.
29 § 31-32-2.
30 § 31-27-2 (k).
31 § 31-30-4, [17] and § 31-32-1, [20].
32 § 31-30-4, [17].
33 § 31-31-10, [42].
34 § 31-29-6, [54].
35 § 31-31-11, [43].
36 § 31-29-6, [54].
37 § 31-32-3, [63].
38 § 31-32-4, [64].
39 § 31-32-5, [65].
40 Professor Clark advised the legislative interim committee: "The definition of 'earned surplus' in subparagraph 1 is based on a definition of that term originally formulated by a committee of the American Institute of Accountants in 1930. Rather than use a balance sheet test of earned surplus, the Model Act definition of the term refers to net profits and income over the history of the corporation. This comes from the profit and loss statements of the corporation rather than from the balance sheet. Any additional surplus not traceable to the profit and loss account of the corporation, is defined in subparagraph m as a capital surplus." Memorandum of August 14, 1957, to Legislative Interim Committee.
41 § 31-32-6, [66].

Earned surplus is one of the concepts employed in determining the right of a corporation to purchase its own shares[42] and the right of the board of directors to declare cash or property dividends.[43] The board of directors may transfer earned surplus to stated capital[44] or to capital surplus.[45]

Capital surplus may arise from the sale of par value shares for more than par, or from an allocation to capital surplus of not more than twenty-five per cent of the consideration received for no par shares.[46] It may result from a conversion of shares,[47] a reduction of stated capital, or a transfer from earned surplus.[48] It may be decreased by a conversion of shares [49] and by a distribution in partial liquidation to shareholders.[50] It may be used to purchase the corporation's own shares, if authorized

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42 § 31-28-2, [5].
43 § 31-31-10, [42].
44 § 31-32-1, [20].
45 § 31-32-6, [66].
46 § 31-32-1, [20].
47 § 31-30-4, [17].
48 § 31-32-5, [65] and § 31-32-6, [66].
49 § 31-30-4, [17].
50 § 31-31-11, [43].

by the articles of incorporation or if approved by two-thirds of the outstanding shares entitled to vote,[51] or to decrease or eliminate a deficit.[52]

The term "insolvent" is not presently defined in Colorado law.[53] The term is defined in the new law in its equity sense as opposed to the bankruptcy sense.[54] A corporation is insolvent in the equity sense when it is unable to meet its obligations as they become due. It is insolvent in the bankruptcy sense when its total liabilities exceed its total assets.

CORPORATE POWERS AND LIMITATIONS

A. POWERS

Every corporation organized under the Colorado Corporation Act will have the powers set forth in section 4 of the act. None of these powers need be set forth in the articles of incorporation.[55]

Every existing Colorado corporation to which the new law will become applicable automatically will acquire whatever change or increase in its statutory general powers appears by comparing the new section 4 with the old section 31-1-19.[56]

Generally, the following present powers continue: to have perpetual succession, to sue and be sued, to have a corporate seal, to acquire, purchase, own, lease, mortgage, and convey real and personal property, to borrow money, to appoint officers and agents and fix their compensation, to adopt and change by-laws, to dissolve, to conduct business and maintain offices outside Colorado, and to make donations. However, the more elaborate language which the new law uses to set forth such powers suggests that Colorado lawyers would be well advised to consider carefully those subsections of the new law which set forth those powers.[57]

In addition, the following subsections of section (4) are set forth at length because they definitely will constitute an extension of new corporate powers to existing Colorado corporations on January 1, 1959:

> "(f) To lend money to, to guarantee the obligations of and to otherwise assist its employees and, upon the affirmative vote of two-thirds (⅔) of its stockholders, to lend money to, to guarantee the obligations of and to otherwise assist its directors and officers, but no loans shall be made by a corporation secured by its shares.
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> "(i) To lend money and to guarantee the obligations of others for its corporate purposes, to invest and reinvest its funds and

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51 § 31-28-2, [5].
52 § 31-32-6, [66].
53 Professor Clark stated: "The present Colorado Statute contains no definition of insolvency and where that term is used its meaning has to be gathered from the context. For example, in the present Colorado dividend provision which is Colorado Revised Statutes 31-2-12, insolvency probably means equity insolvency since only that meaning makes sense in that section. But there is still no clear indication that that is what the legislature intended." Memorandum of Aug. 14, 1957 to the Interim Committee.
54 § 31-27-2 (n), [2 (n)].
55 § 31-29-2, [50].
56 Colo. Rev. Stat. § 31-1-19 (Supp. 1957).
57 § 31-27-4 (a), (b), (c), (d), (e), (g), (h), (j), (k), (l), (m) and (q).

to take and hold real and personal property as security for the payment of funds so loaned or invested, or as security for the obligations of others to it.

"(n) In time of war to transact any lawful business in aid of the United States in the prosecution of the war.

"(o) To indemnify any director or officer or former director or officer of the corporation, or any person who may have served at its request as a director or officer of another corporation in which it owns shares of capital stock or of which it is a creditor, and the personal representatives of all such persons, against expenses actually and necessarily incurred by him in connection with the defense of any action, suit or proceeding in which he is made a party by reason of being or having been such director or officer, except in relation to matters as to which he shall be adjudged in such action, suit or proceeding to be liable for negligence or misconduct in the performance of duty; but such indemnification shall not be deemed exclusive of any other rights to which such director or officer may be entitled, under any by-law, agreement, vote of shareholders, or otherwise.

"(p) To pay pensions and establish pension plans, pension trusts, profit-sharing plans, stock bonus plans, stock option plans and other incentive plans and to provide medical service, life, sickness, accident, disability or unemployment insurance, education, housing, social and recreational services, and other similar aids and services for all or any of the directors, officers and employees of the corporation, or of any subsidiary thereof, wholly or partly at the expense of the corporation.

"(r) To enter into general partnerships, limited partnerships (whether the corporation be a limited or general partner), joint ventures, syndicates, pools, associations and other arrangements for carrying on of one or more of the purposes set forth in its articles of incorporation, jointly or in common with others.

"(s) To have and exercise all powers necessary or convenient to effect any or all of the purposes for which the corporation is organized."

The powers described in subsections (a), (c), (d), (e), (g), (h), (j), (k), (l), (m), (n), and (q) of the new section 4 are the same as the corresponding subsections of the Model Act; subsection (s) is the same as subsection (r) of the Model Act.

The first material departure from the Model Act appears in subsection 4 (f). That provision, as enacted, is the result of careful reconsideration by the legislative interim committee after an earlier draft met adverse criticism from Professor Clark.[58] It should be noted that the Model Act's prohibition against a corporation making loans secured by its shares[59] was retained in the Colorado version.[60]

Subsection 4 (o) of the Model Act relating to indemnification of officers and directors appears to have been taken bodily from Delaware law. It was later changed in the 1957 revisions to the Model Act. The Colorado subsection, however, is substantially the same as the 1953 Model Act revision. This subsection has been criticized on the ground that it enables directors and officers who may have engaged in wrongdoing and are sued, to settle such cases for substantial amounts and charge the settlement to the corporation.[61] Professor Clark suggested some safeguards, such as requiring court approval of settlements and indemnification. He also suggested that it would be desirable to require management to notify the shareholders of any settlements.

Subsection 4 (p) is an extremely broad grant of power to a corporation. A provision of the Virginia law which empowered corporations to insure the lives of officers and directors has been criticized on the ground that there was no requirement of benefit to the corporation.[62] This allows executives to designate wives and beneficiaries other than the corporation and so indirectly authorizes additional compensation to such executives.

Subsection 4 (r), which empowers corporations to enter into partnerships, syndicates and other joint arrangements, is not found in either present Colorado law or in the Model Act.[63]

B. RIGHT OF A CORPORATION TO ACQUIRE AND DISPOSE OF ITS OWN SHARES

A corporation under the new law[64] will have the right to acquire and dispose of its own shares to the extent of the earned surplus and capital surplus available for this purpose, subject to the limitation that no purchase can be made when the corporation is insolvent or would become insolvent. A second limitation is expressed in the following words:

> "To the extent that earned surplus or capital surplus is used as the measure of the corporation's right to purchase its own shares, such surplus shall be restricted so long as such shares are held as treasury shares, and upon the disposition or cancellation of any such shares the restriction shall be removed pro tanto."[65]

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[58] Professor Clark informed the interim committee that section 4 (f): "has been severely critized in an article, Harris, 'The Model Business Corporation Act—Invitation to Irresponsibility', 50 Northwestern University Law Review 1, 3 (1955). The author of this article suggests that there is no definition of the word 'assist', used in this subparagraph, and that it gives the corporate management much too broad a power to benefit themselves at the expense of the shareholders." Memorandum of Aug. 14, 1957 to Interim Committee.

[59] Model Business Corporation Act § 42 (rev. 1953).

[60] § 31-27-4 (f), [4 (f)].

[61] Emerson, supra note 13 at 499 to 501.

[62] Id. at 502.

[63] On this subsection, Professor Clark advised the interim committee: "The law has in the past been that a corporation could not be a partner because of the delegation of authority that would involve to the other partners to bind the corporation in partnership transactions. Allowing entry into a general partnership is, I think, in line with the modern trend." Memorandum of Aug. 14, 1957, to the Interim Committee.

[64] § 31-28-2, [5].

[65] § 31-28-2 (b), [5 (b)].

Such limitations, however, do not apply when a corporation acquires its own shares to eliminate fractional shares. to collect or compromise debts, to pay dissenting shareholders, or, subject to the other provisions of the act, to retire its redeemable shares by redemption or by purchase at not to exceed the redemption price.

Section 5 was one of the few on which the legislative interim committee and the bar association committee did not readily agree. Some members of the interim committee desired to limit the right of a corporation to purchase its own stock out of capital surplus in the manner that such right is limited in the Model Act; by requiring the articles to allow it, or requiring a two-thirds vote of shareholders. On the other hand members of the bar association committee argued that such limitations should not be enacted because under present Colorado case law a corporation probably has a right to purchase its own shares out of capital surplus.[66]

With respect to the matter of accounting for treasury stock, the bar association committee referred the matter to the Colorado Society of Certified Public Accountants; the President of the Society appointed a committee to consider the matter. Thereafter, Mr. Thomas E. Stanley, representing the accountants' committee, informed the bar association committee as follows:

> "Section 2 (m) defines Capital Surplus as 'the entire surplus of a corporation other than its earned surplus,' thus it seems that appraisal or donated surplus would be included in capital surplus. Is this the intent of the act? In arriving at

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[66] With respect to this section, Professor Clark advised the interim committee: "This is an important provision and relates back to the definition of 'earned surplus' found in section 2 (1) . . . . The present Colorado Statute on the purchase by the corporation of its own shares is in Colorado Revised Statute 31-1-25 (1953). This statute allows the corporation to purchase all classes of its own shares, provided that this cannot be done when that would cause an impairment of the capital of the corporation. The intent of this existing statute is clear enough, namely, to make sure that there is at least some sort of a surplus sufficient to cover the purchase by the corporation of its own shares. This statute has in effect been nullified by Colorado Industrial Loan and Investment Co. v. Clem, 82 Colo. 399 (1927). This case held that there was no restriction of such purchases to surplus and that there could be no impairment of the company's capital by the purchase of the shares, even if no surplus was available, because after the purchase the company would hold the stock in the treasury and could sell it at any time. In such a case the court reasoned the shares become part of the company's property and should be held like any other asset of the corporation. This, of course, is a complete misunderstanding of the status of shares of a corporation purchased and held in its treasury.

"The proposed change in the statute is therefore certainly desirable provided that one approves of the source of the funds, namely, 'earned surplus' as defined. The Model Corporation Act allows purchase of the corporation's own shares only out of earned surplus except that capital surplus may also be used either if the articles of incorporation allow it, or if it has been approved by a vote of two-thirds of all shares entitled to vote. The proposed Colorado Statute does not contain the limitation on the use of capital surplus for this purpose, but apparently allows either earned surplus or capital surplus to be used. It would seem to me that this is undesirable. It would allow a corporation to issue its shares at a price substantially above par, or above a stated amount as to no par shares, and then use the capital surplus so created to buy back the shares of certain individuals without any notice in advance to the shareholders that this might be done, or without any vote by the shareholders. This opens the way to possibilities of abuse, and I think, at the very least, the safeguards found in Section 5 of the Model Act should be retained. Subsection b of section 5 makes it clear that shares held as treasury shares are not to be treated like assets of the corporation, but are to effect a restriction on the surplus used to purchase them. This subsection overrules the Clem case and brings the treatment of treasury shares into line with at least some segments of accounting opinion." Memorandum of Aug. 14, 1957, to the Interim Committee.

accounting procedures for treasury stock, our committee assumed the usual situation in which capital surplus has been created by the sale of capital stock for more than the par value or stated value.

"We believe that in general capital surplus available for purchase of treasury stock should be limited to the capital surplus arising from issue of the particular class of stock being repurchased, thus retaining in capital stock or capital surplus the total proceeds from issue of the other classes of stock. In some cases it might be possible to consider all of the capital surplus applicable to a class of stock as available for repurchase of only a portion of that class, however, generally we believe it should be considered available only to the extent of the capital surplus applicable to the number of shares being repurchased.

"One other question was raised by our committee. In section five, do the words 'direct or indirect' restrict a subsidiary from purchasing shares of the parent, unless the parent has sufficient surplus to meet requirements of the act?

"As to the accounting for treasury stock our committee believes the following procedures should be followed:

"1. Purchase or other acquisition of treasury stock should be charged to the treasury stock account at cost.

"2. (a) Upon sale of treasury stock at a profit the portion of the proceeds representing cost should be credited to the treasury stock account and any excess should be credited to capital surplus."

"2. (b) In case of sale at less than cost, the cost in excess of selling price should be charged to capital surplus to the extent available for the particular stock, and any balance should be charged to earned surplus.

"3. On cancellation of treasury stock, the cost should first be applied to par value or stated value as the case may be, then to capital surplus to the extent available and any balance should be charged to earned surplus.

"4. We believe treasury stock should be shown on the balance sheet in either of two ways:

1. All surplus accounts should be listed and totaled and the cost of treasury stock deducted therefrom, extending the net balance as surplus in the capital section.
2. All stated value (capital stock) and all surplus accounts may be totaled and the cost of treasury stock deducted from such total to determine net capital. If this method is used and the cost of treasury stock is a material amount, disclosure should be made of the amount of restriction on capital surplus and earned surplus.

"With reference to shares acquired under section 5 (b) (1) (2) and (3) we assume such shares remain treasury shares until cancelled by board of directors, in which case accounting would be the same as for other treasury shares, if the Act contemplates immediate cancellation on acquisition then the original entry should be the same as cancellation entries previously stated. We understand that shares acquired under section 5 (b) (4) become cancelled on acquisition."[67]

C. OTHER PROVISIONS ON POWERS AND LIMITATIONS

(1) *Ultra Vires*

Section 6 of the new law[68] attempts to minimize the defense of ultra vires as to corporations subject to the act, except where an action is brought by a shareholder of the corporation (subsection (a)), by the corporation (subsection (b)), or by the Attorney General (subsection (c)). Section 6 does not distinguish between complete lack of power and abuse of power, and does not distinguish between express powers and implied powers. Likewise, the section does not give effect to performance by either party, except in cases governed by clause (a).[69]

(2) *Corporate Names*

A corporation's name may not contain any word or phrase which indicates that it is organized for any purpose other than one of the purposes contained in its articles, nor can it be the same as or deceptively similar to the name of any domestic corporation, any foreign corporation authorized to do business in Colorado, any name which is reserved, any name which is registered under the provisions of the new law,[70] or any trade mark and business name which is registered under Colorado law.[71] A name can be reserved for 120 days upon filing an application with the Secretary of State at a cost of five dollars.[72] Any foreign corporation can register its name by filing with the Secretary of State an application and a certificate of good standing executed by the Secretary of State of the state in which it is organized. Such registration is effective until the close of the calendar year in which the application is filed (at a cost of one dollar for each effective month),[73] and may be renewed from year to year.[74]

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67 Letter from Thos. E. Stanley to Charles Baer, Oct. 2, 1957.

68 § 31-28-5. The Colorado section follows the Model Act.

69 With reference to this section Professor Clark stated: "This section places in the statute what I think most people have come to believe is the correct treatment of the troublesome problem of ultra vires. I do not believe that this section really changes Colorado case law, but it places that case law in statutory form so that it can be readily found and relied on by the persons concerned. For example, I think it is pretty clearly the law in Colorado that the corporation cannot set up the defense of ultra vires when it is sued for breach of contract, if it has received all or part of the performance from the other contracting party. On this point, see Mulford v. Torrey Exploration Company, 45 Colo. 81 (1909) and Colorado Industrial Loan Co. v. Clem, 82 Colo. 399 (1927), noted in 1 Rocky Mt. Law Rev. 20." Memorandum of Aug. 14, 1957 to Interim Committee.

70 § 31-28-6, [7].

71 Colo. Rev. Stat. Ch. 141 (1953).

72 § 31-28-7, [8]; § 31-36-4 (e), [123]. Cf. Colo. Rev. Stat. §§ 31-1-3 and 31-1-4 (1953).

73 § 31-28-8, [9].

74 § 31-28-9, [10].

(3) *Secretary of State*

The Secretary of State is given power to administer the Colorado Corporation Act.[75] He has the power to propound interrogatories which must be answered within thirty days unless an extension of time is granted.[76] Such interrogatories and the answers are not open to public inspection.[77] The Secretary of State is required to give written notice within ten days of his disapproval of any document submitted to him for filing. Such disapproval can be appealed to the district court[78] where a trial *de novo,* rather than simply a review of the secretary's action,[79] can be had to determine whether the secretary has legally pursued his authority. Reports required to be filed in the office of the Secretary of State are required to be made on forms prescribed and furnished by him.[80]

(4) *Registered Office and Registered Agent*

Each corporation organized under the new act must set forth in its articles[81] the address of its initial registered office and the name of its initial registered agent at such address. The new act requires each domestic[82] and foreign[83] corporation to have and continuously maintain a registered office and a named agent (either an individual or corporation) at such office.[84] This is primarily for convenience in the service of process.

The new law does not specifically require that existing corporations, either domestic or foreign, file a statement showing the name and address of the registered agent and office. Because such information must be set forth in annual reports which must be delivered to the Secretary of State between January 1 and May 1 of each year, the bar association and interim committees considered that it would be sufficient if such information was submitted in the annual report for 1958. The Secretary of State, however, on the basis of the penalty provisions, in October, 1958, planned to mail a form to each corporation on which it could file a statement as to its registered office and agent.

If a domestic[85] or foreign[86] corporation fails to appoint or maintain a registered agent in Colorado or if its registered agent cannot be

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[75] § 31-28-15, [133].

[76] § 31-28-13, [131]. § 31-36-11, [129] provides that each corporation that fails to answer interrogatories shall be deemed guilty of a misdemeanor and upon conviction thereof may be fined in any amount not exceeding five hundred dollars.

[77] § 31-28-14, [132].

[78] § 31-28-16, [134].

[79] Cf. Colo. Rev. Stat. § 31-1-9 (1953).

[80] The Colorado Bar Association has been working with the Secretary of State's office to develop appropriate forms and such forms will be made available to the public.

[81] § 31-29-2 (j), [50].

[82] § 31-28-10, [11].

[83] § 31-35-17, [108].

[84] There are no equivalent requirements in the present Colorado law. A domestic corporation in its certificate of incorporation is now required to set forth the town or city or county in which its principal office is located. Colo. Rev. Stat. § 31-1-6 (6) (1953). Since no street address is required there is not the clear equivalent of a registered office. A domestic corporation is required to designate one or more process agents in its annual report only if it is created to carry on business outside of Colorado or if its books may be kept outside the state. Id. § 31-1-11. Many domestic corporations do not have a process agent.

[85] § 31-28-12, [13].

[86] § 31-35-19, [110].

found at the registered office, then process may be served on the Secretary of State. Failure by a domestic corporation to appoint and maintain a registered agent for thirty days or to file a statement of change of its registered office or agent is cause for involuntary dissolution.[87] The same failures by a foreign corporation are causes for revocation of its certificate of authority to transact business in Colorado.[88]

Involuntary dissolution requires the Secretary of State to certify such failure to the Attorney General, who, not less than thirty days after the receipt of such certification, is required to file an action against the corporation for its dissolution. The Secretary of State, is also required to mail to the corporation at its registered office a notice that the certification has been made. If the corporation complies before the Attorney General files the action, the complaint will not be filed. If the action already has been filed, the corporation is required to pay the costs and a penalty of fifty dollars. Then the action abates.

A foreign corporation may have its certificate of authority to transact business in Colorado revoked by the Secretary of State after sixty days notice, if it fails to appoint and maintain a registered agent in Colorado.[89] However, as foreign corporations have been required by law to file a certificate designating the principal place where the business shall be carried on in Colorado and naming an authorized agent in Colorado residing in the county fixed for its principal place of business, it appears that the Secretary of State would be overly technical if he attempted to impose any sanctions on an existing foreign corporation which fails to notify the Secretary of State of its registered office and registered agent otherwise than by reporting such information in its annual report for 1958. In view of the sixty days notice requirement before the Secretary of State can revoke a certificate of authority of a foreign corporation, it appears that existing foreign corporations which can expect to receive notice at the address of their present authorized agent will have adequate time within which to avoid any sanctions that the Secretary may attempt to impose.

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87 § 31-34-13, [90].
88 § 31-35-16, [116].
89 § 31-35-12, [116]. If the corporation's authority to transact business in Colorado is revoked, it loses its right to sue but not to defend. § 31-35-13, [117]; § 31-35-3 [119].

ARTICLES OF INCORPORATION AND AMENDMENTS

A. ARTICLES

Under the new law[90] any three or more natural persons twenty-one years of age or older may act as incorporators. They need not be residents of Colorado or citizens of the United States and need not be subscribers to shares in the corporation. After they sign, verify and deliver articles of incorporation, in duplicate, to the Secretary of State, their only remaining function is to call an organization meeting of directors,[91] or, under specified conditions, to dissolve the corporation.[92]

The Model Act provision relating to the contents of the articles of incorporation was recommended to the bar association committee as an improvement over the rather antiquated provision in the present law.[93] The Colorado Corporation Act, however, omitted the Model Act requirement[94] that the articles contain a statement that the corporation will not commence business until at least one thousand dollars has been received for the issuance of shares, and inserted in lieu thereof a requirement that the articles of incorporation set forth:

> "(g) Provisions relating to cumulative voting: (1) For corporations organized subsequent to December 31, 1958, if cumulative voting is not desired in the election of directors a statement to that effect shall be made; if no such statement is made cumulative voting shall be mandatory in the election of directors. (2) For corporations organized prior to January 1, 1959, the certificate of incorporation shall state whether or not cumulative voting shall be allowed in the election of directors or trustees. In case the certificate of incorporation of the company permits cumulative voting stockholders shall be permitted to cumulate their shares in the election of directors as provided in Section 32 hereof."[95]

In preparing articles of incorporation, reference should be made to the various substantive provisions applicable to the items required to be set forth in the articles. For example, reference should be made to section 7,[96] with respect to the name; to section 3,[97] for the corporate purposes; and to sections 14,[98] and 15,[99] for matters relating to shares

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[90] § 31-29-1, [49]. Cf. Colo. Rev. Stat. § 31-1-2 (1953).
[91] § 31-29-5, [53].
[92] § 31-34-1, [77].
[93] § 31-1-6.
[94] Model Bus. Corp. Act § 48 (g). In Ballantine, Corporations, 84 (1946), it is stated: "Under the statutes of many states the subscription and payment of a minimum capital, usually of nominal amount, are required before the transaction of business. If business is done without such provision of capital the directors and sometimes shareholders or even incorporators are expressly made liable to creditors. The attempt to do corporate business without providing in good faith any sufficient basis of financial responsibility may be regarded as a fraud upon creditors, an abuse of the separate corporate entity privilege, independent of statute." Colorado statutes have never contained such a requirement.
[95] §31-29-2, [50]. The first sentence of (2) in the text quotation was taken directly from Colo. Rev. Stat. § 31-1-6 (12) (1953), which has been law in Colorado since 1931.
[96] § 31-28-6.
[97] § 31-27-3.
[98] § 31-30-1.
[99] § 31-30-2.

Duplicate copies of the articles of incorporation must be delivered to the Secretary of State for filing.[100] The requirement of the present law[101] that a certified copy of the certificate of incorporation be filed in any county in which the corporation may own real estate has been eliminated. It would appear advisable to continue this practice, however, for purposes of a good record title.

Corporate existence begins upon issuance of the certificate of incorporation by the Secretary of State.[102] Thereafter a majority of the incorporators are required to call an organization meeting of the directors to adopt by-laws, elect officers, and transact such other business as may come before the meeting.[103]

B. AMENDMENTS TO ARTICLES

Section 54 of the new law, relating to the right to amend articles of incorporation[104] is identical to the corresponding section of the Model Act with the exception of subsection 54 (p). Several changes from the Model Act were made with respect to procedure, however. The requirement that the board of directors adopt a resolution and submit it to the shareholders was retained.[105] In addition, the holders of at least one-tenth of the outstanding voting shares can request the president to call a special meeting of shareholders to consider an amendment.[106] In either event, written notice of the amendment must be given, and, because of a peculiar provision of the Colorado Constitution,[107] at least thirty days' notice must be given if a change in the amount of outstand-

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[100] § 31-29-3, [51].

[101] Colo. Rev. Stat. § 31-1-7, (1953).

[102] § 31-29-4, [52], Cf. Colo. Rev. Stat. § 31-1-10 (1953) which is very similar. Concerning this section, Professor Clark advised the legislative interim committee: "This section is drafted with the view of at least minimizing the old de facto incorporation problem, by making the issuance of a certificate of incorporation conclusive evidence that proper incorporation has occurred. Until that certificate is issued, there is no incorporation and presumably the individuals involved in the enterprise would be personally liable for debts of the enterprise." Memorandum of Aug. 14, 1957, to Interim Committee.

In an address to the Colorado Bar Association in October 1956, Mr. Ray Garrett, Chairman of the A.B.A. Committee on Corporate Laws, stated: "The de facto doctrine which bothered you so much in law school disappears for all practical purposes in the procedure prescribed in the Model Act. When the Secretary of State issues a charter, the corporation is de jure. Prior to that, there isn't a corporation, de facto or otherwise. The de facto doctrine no doubt grew up in those early days when you first got a license to solicit subscriptions, then you went about it, and then you finally filed your charter papers. Meanwhile, you had a de facto existence. It is hardly possible to have a de facto corporation under the Model Act. It would have to be something extremely fraudulent in the initial documentation because the first thing you file is the Articles of Incorporation."

[103] § 31-29-5, [53]. It appears that the three days notice by mail required by § 31-30-19, [138] can be waived.

[104] § 31-29-6, [54]. Professor Clark stated to the interim committee: "The power to amend given by this section is no broader than the one in the existing statute which is Colo. Rev. Stat. § 31-3-1 (1953). The only question raised here is as to the validity of such broad powers to amend. There is authority to the effect that there are some restrictions on the power which can be given by the legislature to one group in the corporation as against another, to amend the charter in ways which would adversely affect the rights of some shareholders. In spite of these cases, it is customary nowadays to give by charter very broad amendment powers and I would not raise any objection to this section on that account. I merely point out that there is a constitutional question. Cases on this are collected in the following annotations: 105 ALR 1452, 1453-1457 (1936); 117 ALR 1290 (1938); 8 ALR2nd 893, 900-902 (1949)." Memorandum of Aug. 14, 1957, to Interim Committee.

[105] § 31-29-7, [55].

[106] § 31-30-11, [27]. Cf. Colo. Rev. Stat. § 31-3-2 (1953). Note the reduction from the one-third requirement of prior law.

[107] Colo. Const. art. XV, § 9 (1876).

ing stock is proposed. Shareholders must either adopt or reject an amendment submitted by the board of directors; they cannot revise it. An amendment requires the affirmative vote of at least two-thirds of the shares entitled to vote, or two-thirds of the shares of any class entitled to vote as a class and two-thirds of the total shares entitled to vote.[108] The Model Act provision as to class voting on amendments was adopted without change in Colorado.[109] The same is true of the provisions relating to the contents of the articles of amendment,[110] the filing of such articles with the Secretary of State,[111] and the effect of issuance of a certificate of amendment.[112]

Provisions of the present law[113] relating to composite articles of incorporation were retained[114] in preference to the provision of the Model Act relating to re-stated articles of incorporation.[115]

The new law contains a special provision[116] for amending articles of a corporation as to which a plan of reorganization has been confirmed by decree or order of court. It is the same as the Model Act, except that a recitation of the particular types of amendments which can be made was omitted as unnecessary.

SHAREHOLDERS AND SHARES OF STOCK

A. SHARES—AUTHORIZED, ISSUANCE, SUBSCRIPTION, CONSIDERATION, PAYMENT, STOCK RIGHTS AND OPTIONS, EXPENSES OF ORGANIZATION, CERTIFICATE FORMS, FRACTIONAL SHARES, PREEMPTIVE RIGHTS

Section 14 of the new law[117] is the basic authority for the issuance of shares by a corporation. It allows division of shares into one or more

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108 § 31-29-7 (c), [55 (c)]. The conflict between Colo. Rev. Stat. § 31-3-3 (1953) (which requires a two-thirds vote) and Id. § 31-4-1 (which requires a three-fourths vote) will soon be resolved.
109 § 31-29-8, [56]. But see Emerson, supra note 13 at 529.
110 § 31-29-9, [57].
111 § 31-29-10, [58].
112 § 31-29-11, [59].
113 Colo. Rev. Stat. §§ 31-1-8 and 31-1-9 (1953).
114 § 31-29-12, [60].
115 The drafting of composite articles is a ministerial job which could not be acted upon intelligently by shareholders unless all of the documents were presented to them, in which case it would become a mere proof-reading operation.
116 § 31-29-13, [61].
117 § 31-30-1.

classes, with or without par value, and with such designations, preferences, limitations and relative rights as are stated in the articles of incorporation. The articles may limit or deny voting rights to the shares of any class, to an extent not inconsistent with the provisions of the act. This section is identical to the 1953 Model Act provision. The shares of any preferred or special class may be divided and issued in series. Relative rights and preferences as between different series may be fixed and determined by the articles of incorporation in certain listed particulars. The directors, if allowed by the articles, can divide the classes into series within the limitations of the act and the articles.[118] The Colorado provision follows the Model Act, except that in Colorado variations between different series may be made with respect to the time of paying dividends, the date from which dividends will be cumulative, and voting powers, if any.[119] The issuance of preferred shares in series facilitates the raising of capital from time to time under current market conditions, but the power to issue in series is expressly limited in order to protect outstanding shares of the same class.

Under the new law[120] pre-incorporation subscriptions to shares are irrevocable for six months unless otherwise provided in the subscription agreement or by consent of all subscribers. The six months provision will no doubt be welcomed by promoters.

The Model Act provision relating to consideration for shares has been adopted in Colorado.[121] Par value shares may be issued for not less than par, while no par and treasury shares may be issued for such consideration expressed in dollars as may be determined by the board of directors. A clear distinction is made between a share dividend and a split-up of shares.[122] A share dividend requires a transfer of surplus to stated capital as consideration for the shares issued. No transfer of surplus to stated capital is required in a split-up of shares. The consideration for the issuance of shares may be property, tangible or intangible, money, or labor or services actually performed for the corporation. However, neither promissory notes nor future services will constitute payment. In the absence of fraud, the judgment of the directors or the shareholders, as the case may be, as to the value of the con-

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[118] Professor Clark advised the Interim Committee: "The comparable section of the existing Colorado Statutes is 31-1-14 (1953). The proposed section, as does the existing Colorado law, authorizes the so-called 'blank share,' if the articles of incorporation allow it. The blank share is a share as to which the directors may establish rights and preferences without having those rights and preferences spelled out in the articles of incorporation. In order to use blank shares, the articles of incorporation must expressly give this authority to the board of directors and their authority to vary the rights and preferences is, of course, limited by this section of the statute. The new proposed statute, in line with the Model Act, provides the additional safeguard not found in the existing law that before there can be any issue of blank shares, the corporation must file a statement in the Secretary of State's Office giving various information about the corporation and the resolution establishing the shares." Memorandum of August 14, 1957, to the Interim Committee.

[119] The Colorado Bar Association committee was advised that many states provide that the board of directors may fix the rate of dividend and dividend payment date. This, it was stated, avoids the necessity of purchasers having, under certain circumstances, to pay a large amount of accrued dividends upon the purchase of preferred stock. It was also noted that insurance companies in particular do not like to make large payments of this character.

[120] § 31-30-3, [16].

[121] § 31-30-4, [17].

[122] § 31-31-10, [42].

sideration received for the shares is conclusive.[123] The Colorado provision is the same as the Model Act, except that it contains additional language which is italicized in the following sentence:

"When payment of the consideration for which shares are to be issued shall have been received *in an amount not less than par value or stated value* by the corporation, such shares shall be deemed to be fully paid and nonassessable."[124]

The provision of the new law relating to stock rights and options[125] follows the Model Act, except that it has omitted the Model Act requirement that issuance of such rights or options to directors, officers or employees of the corporation must be approved by a majority of the outstanding shares. Here again, in the absence of fraud, the judgment of the board of directors as to the adequacy of consideration is conclusive.

The reasonable charges and expenses of organizing a corporation may be paid by the corporation out of the consideration received for its shares without rendering the shares not fully paid and non-assess-

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[123] § 31-30-5, [18]. Professor Clark advised the Legislative Interim Committee with respect to this and the preceding section as follows: "This section is really concerned with the watered stock problem, which under the existing law is covered in four different places in the statutes. These sections are Colorado Revised Statutes, § 31-1-26, which provides that no corporations shall issue stock or bonds except for labor done, services performed, for money or property actually received, and that all fictitious increase of stock or indebtedness shall be void; Colorado Revised Statutes 31-1-16, which allows the purchase of property for stock to the amount of the value thereof; Colorado Revised Statutes 31-2-13, providing that each stockholder shall be liable for the debts of the corporation to the extent of the amount that may be unpaid on the stock held by him; and, finally, Colorado Revised Statutes 31-6-8, which provides that if any corporation allows an execution to be returned with no property found or remain unsatisfied for ten days, suits in equity may be brought against stockholders or other persons liable for the debts of the corporation, and they may be required to pay such debts. The leading case in Colorado on all these matters is Frink v. Carman Co., 97 Colo. 211 (1935), which held that a shareholder who received 100 shares of common stock as a bonus when he bought 100 shares of preferred, was liable to a creditor of the corporation for the par value of the common even though he had an agreement with the corporation itself that the common stock should be fully paid and non-assessable. This case placed Colorado in the minority of jurisdictions following Easton National Bank v. American Brick and Tile Co., 70 N.J. Eq. 732, 64 Atl. 917 (1906). This case held that under the New Jersey statute any shareholder who took bonus, discount, or watered stock would be liable to all creditors of the corporation for the full par value of his shares.

"Another Colorado case on this point is Buck v. Jones, 18 Colo. App. 250 (1902), reaching a similar result.

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"I would suggest that first of all, there should be consideration of precisely what protection the creditors should be given against watered stock. Secondly, the new legislation should be drafted to make the scope of protection, if any, clear. Article XV, Section 9 of the Colorado Constitution, making void 'all fictitious increase of stock or indebtedness,' should also be considered. I would at least question whether section 18 of the proposed statute does not violate this constitutional provision.

"The last paragraph of section 18 makes the judgment of the directors as to valuation of property received for shares conclusive in the absence of fraud. This is probably the same rule as now exists under case law in Colorado. The case on this is Speer v. Bordeleau, 20 Colo. App. 413 (1905). This case held that where a creditor is asserting that shares were issued for over-valued property, he has the burden of showing that the over-valuation was intentional and fraudulent on the part of the directors. Some confusion has been caused by a later case in Colorado, Bernard v. Sweet, 74 Colo. 302 (1923), which held directors liable where they had no reasonable grounds for their belief as to value, and this may qualify the broad rule of the Speer case. In any event, probably the proposed statute does not work any great change on this point."

[124] The italicized language was added in an effort to eliminate, so far as possible, the issuance of watered, discount or bonus shares.

[125] § 31-30-6, [19].

able.[126] Colorado adopted the Model Act provision relating to the form of certificates representing shares.[127] The new law also authorizes the issuance of fractional shares or script.[128]

The section of the new law relating to shareholder's preemptive rights and employee stock plans represents a substantial change from the Model Act provision. Under the Colorado version[129] the preemptive right of a shareholder to acquire unissued or treasury shares also applies to securities convertible into shares or securities carrying stock purchase warrants or privileges. Under both the new law and the Model Act such preemptive right may be limited or denied by the articles.

If a majority of the stockholders approve, a corporation may sell shares to, grant stock rights or options to, or establish stock bonus and other incentive plans for the benefit of its directors, officers and employees, without first offering such shares, rights, options, or plans to its shareholders. If, however, the corporation concurrently offers to sell its shares to the public or its shareholders, then approval by a majority of the stockholders is not required provided the shares sold to the directors, officers and employees do not exceed ten per cent of the number offered to the public or its shareholders at the same price. The limited grant of authority contained in this section should be compared with the general and unlimited grant of authority with respect to stock bonus

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[126] § 31-30-7, [21]. This section removes any doubt as to the power of a corporation to pay its own expenses of incorporation and of the underwriting of its shares. Presumably, this section would authorize a corporation to issue shares to the underwriters or to the promoters in payment for their pre-incorporation expenses provided a reasonable value were placed on those services and expenses.

[127] § 31-30-8, [22]. Professor Clark advised the Interim Committee: "I have not found in the existing Colorado Statutes any comparable section. This one has been criticized in 50 N.W. Univ. Law Rev. 1, 11 (1955) on the ground that the share certificate does not give the shareholder any information about the preferences and relative rights which go on his shares, or in the alternative that it does not require the corporation to furnish him, on its own motion, with that information. It merely notifies him that he may find out these facts by making a request to the corporation. I do not know that this is a very serious criticism of the section, though of course it does put on the shareholder the burden of informing himself in a field which perhaps he may not be likely to discharge that burden."

[128] § 31-30-9, [23].

[129] § 31-30-10, [25]. Professor Clark stated to the committee: "The first paragraph of this section announces a rule which is already found in the Colorado Statutes, Colo. Rev. Stat. § 31-1-6 (10) (1953), allowing the shareholder's preemptive right to be limited or denied by the articles of incorporation. . . . It is also important to note that the preemptive right is made applicable to treasury shares, which is presently not the law in Colorado, under the case of Crosby v. Stratton, 17 Colo. App. 212 (1902). The inclusion of treasury shares within the shareholder's preemptive right is usually considered by commentators to be desirable because of the analytical similarity between treasury shares and authorized but unissued shares.

"The second paragraph of this section is somewhat like the present Colorado Revised Statute, § 31-2-18 (1953) allowing employee stock and profit sharing plans to be set up and allowing the shares issued under such plans to be issued free of the ordinary preemptive right. The section as written in the proposed Colorado Statute is somewhat different from the Model Act provision, however. The Model Act provision requires a vote of two-thirds of the shareholders in order to approve such a profit sharing plan, while the provision proposed for Colorado requires only a majority vote. My own preference is for the two-thirds vote because of the possibilities of abuse of such plans by management. The proviso in the Colorado proposal is not found at all in the Model Act. This proviso is not altogether clear, but apparently it is aimed at qualifying the shareholder's preemptive rights as to 10% of any offer made by the corporation to sell shares to the public or its shareholders. I do not see any legitimate purpose for this proviso and would strongly favor eliminating it. If it is desired to have more share ownership in the directors and officers and employees of the corporation, that can be done easily enough by setting up a stock plan and having the shareholders vote on it; and, therefore, the proviso is not needed." Memorandum of Aug. 14, 1957, to Interim Committee.

plans, stock option plans, and other incentive plans contained in section 4(p) of the new law.

B. SHAREHOLDERS' MEETINGS — NECESSITY, NOTICE, WAIVER OF NOTICE, CLOSING OF BOOKS, VOTING LIST, QUORUM, VOTING, VOTING TRUSTS, GREATER VOTING REQUIREMENTS

Under the new law meetings of shareholders may be held at any place, within or without Colorado, as may be provided in the by-laws, but in the absence of a provision, meetings are to be held at the registered office of the corporation. Special meetings can be called by ten per cent of the shareholders entitled to vote.[130] Any action required to be taken at a meeting may be taken without a meeting if unanimous consent is obtained in writing.[131] The requirement for publication of notice of the meeting in the present law[132] will be dropped; the new law merely requires written or printed notice to be delivered not less than ten nor more than fifty days before the meeting either personally or by mail to each shareholder entitled to vote.[133] As under present law, notice can be waived before, at, or after the meeting.[134] Certain special rules governing notice should be kept in mind. At least thirty days notice must be given if the authorized capital stock is to be increased.[135] Specific reference to certain proposed actions must be contained in the notice even though the meeting is not a special meeting.[136]

The section of the new act relating to the closing of transfer books and the fixing of the record date[137] is the same as the Model Act. It provides an orderly method for determining which shareholders are (1) entitled to notice of or to vote at any meeting of shareholders, and (2) entitled to receive dividends.

The voting list must be prepared at least ten days before the meeting, and kept on file at the company's principal office, subject to inspection by any shareholder.[138] A majority of the shares entitled to vote constitutes a quorum. The articles may specify a different fraction, but in no event can the quorum consist of less than one-third of the shares entitled to vote at the meeting.[139] What constitutes a quorum will vary depending upon the business before the meeting. On certain matters all shares are entitled to vote, while on other matters the vote may be restricted by the articles of incorporation. For instance, the articles cannot take away the right to vote on merger and consolidation,[140] sale, mortgage

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[130] § 31-30-11, [27]. At present, meetings of shareholders can be held outside Colorado if the articles so provide. Colo. Rev. Stat. § 31-2-5 (1953). The provision of the new law was adopted from the Model Act.

[131] § 31-30-22, [139].

[132] Colo. Rev. Stat. § 31-2-3 (1953).

[133] § 31-30-12, [28].

[134] § 31-30-19, [138]. Cf. Colo. Rev. Stat. § 31-2-4 (1953).

[135] § 31-30-12. [28]. Colo. Const. art XV, § 9 (1876).

[136] § 31-32-5, [65] (reduction of stated capital); § 31-33-3, [69] (consolidation); § 31-31-12, [75] (sales, mortgage, or lease of assets); § 31-34-10, [84] (revocation of voluntary dissolution proceedings).

[137] § 31-30-13, [29]. See Emerson, supra note 13 at 514, 515. Cf. Colo. Rev. Stat. § 31-2-7 (1953).

[138] § 31-30-14, [30]. See Emerson, supra note 13 at 513. Cf. Colo. Rev. Stat. § 31-2-10 (1953).

[139] § 31-30-15, [31].

[140] § 31-33-3 [69].

or lease of assets,[141] voluntary dissolution,[142] revocation of voluntary dissolution proceedings,[143] or certain amendments to the articles of incorporation.[144] Voting rights may be denied in the election of directors.[145] The section of the new act relating to the voting of shares is

[141] § 31-31-12, [75].
[142] § 31-34-3, [79].
[143] § 31-34-10, [84].
[144] § 31-29-8, [56].
[145] § 31-30-16, [32].

identical to the Model Act, except that fractional shares are entitled to a corresponding fractional vote. Another change was required because of the cumulative voting provision of section 50 (g) of the new law.[146] The new act continues the present Colorado law,[147] authorizing voting trusts for periods not exceeding ten years, but has adopted the wording of the Model Act. The Colorado provision[148] also contains the following sentences which are not found in the Model Act:

> "Each trustee shall maintain at his or its principal office, either within or outside Colorado, such books and records as a corporation is required to maintain under this act. Each beneficiary of the voting trust and his agents and attorneys shall have the same right to inspect such books and records as a shareholder has with respect to the books and records of a corporation under this act."[149]

Colorado has adopted the Model Act provision which authorizes a corporation to impose voting requirements in excess of those required by the act.[150]

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[146] § 31-29-2 (g). According to Emerson, supra note 13 at pages 515-17, it appears that Colorado, New Jersey, Virginia, and Texas have permissive cumulative voting which the author describes as follows: "that is to say, if the management desires to prevent the shareholders from voting cumulatively and so having an opportunity for representation on the board of directors, its corporation counsel simply omits to grant or add cumulative voting rights for shareholders in the articles." Under the new law in Colorado (§ 31-29-2 (g), [50 (g)]) the articles of new corporations must contain a statement whether or not cumulative voting shall be allowed. The new law will make no substantial change.

[147] Colo. Rev. Stat. § 31-2-43 (1953).

[148] § 31-30-17, [33].

[149] This amendment was suggested by Professor Clark's comment, but the first sentence appears to have been written too loosely. Professor Clark advised the Legislative Interim Committee:

"A comment appended to the section of the Model Act dealing with voting trusts states that the holder of a beneficial interest in a voting trust has no right to inspect corporate books and records. I find that highly undesirable and think that such a holder ought to have the right to look at the corporate books. The justification usually advanced for allowing voting trusts is that it is desirable at times to separate the voting rights from the beneficial ownership of shares. If this is so, there does not seem to be any excuse for qualifying other rights which a shareholder may have, such as the right to look at the corporate books and records for a proper purpose. I would therefore recommend a specific provision stating that the shareholder who has deposited his shares in a voting trust and has received a voting trust certificate, should have the right to inspect the corporate records on the same footing as any other shareholder.

"There are a great many other difficulties connected with voting trusts but I suppose they cannot be covered in the statute. For example, suppose the voting trust is set up to continue for the statutory ten year period but a provision for renewal is inserted. Does this make the voting trust invalid or does it make a renewal invalid or can this be done under the statute? Also, there is the question whether the voting trust provision impliedly makes invalid other ways of separating control from ownership such as, for example, the pooling agreement. In some states it has been held that a statute authorizing the creation of a voting trust with certain limitations may impliedly invalidate a pooling agreement where the requirements of the voting trust statute are not complied with. See Ringling v. Ringling Brothers, 49 A.2d 603 (1946), noted in 60 Harv. L. Rev. 651 (1947), as affected by Abercrombie v. Davies, 130 A.2d 338 (Del. Ch. 1957)."

[150] § 31-30-18, [137]. This provision of the Model Act was criticized by Emerson, supra note 13 at page 519, in these words:

"But under the Virginia and Model Act sections a two-thirds majority of the shareholders in a publicly held or other corporation could by amendment of the articles impose on all shareholders greater majority or unanimity requirements. The effect could be to make it impossible for the public or minority shareholders to have any control over the directors, and to make it impossible, as a practical matter, for outside shareholders, for example, to remove the directors, to increase the number of directors, to amend the bylaws or articles, or to otherwise protect their interests and those of the other public or minority shareholders." Emerson quoted the North Carolina version (N.C. Gen. Stat. § 55-66 (a), (b) (Supp. 1955)), and said the New York Stock Corporation Law, particularly its subsections 9 (2) and 9 (3) should be carefully studied for it has much to commend it. See also note 170 infra.

C. LIABILITY OF SUBSCRIBERS AND SHAREHOLDERS AND ACTIONS BY SHAREHOLDERS (DERIVATIVE SUITS)

(1) *Liability of Subscribers and Shareholders*

A holder of or subscriber to shares of a corporation, under the new law[151] is under no obligation to the corporation or its creditors other than to pay the full amount of consideration for which such shares were issued. The consideration for par value shares is par value and the consideration for no par value shares is stated value. This provision is not found in the Model Act. Assignees or transferees in good faith, legal representatives, and pledgees are not personally liable.

(2) *Shareholders Derivative Suits*

The provision of the new law[152] relating to derivative suits is in three parts. Section 45 (a) requires that the plaintiff be a shareholder at the time of the transaction of which he complains, or receive his shares by operation of law from a person who was a holder at such time. This subsection is the same as the Model Act and is substantially the same as Rule 23 (b) of the Colorado Rules of Civil Procedure.

In section 45 (b), the court, upon a finding that the action was brought without reasonable cause, may require the plaintiff to pay to the defendant the costs and reasonable expenses, except attorney fees, directly attributable to the defense.

Section 45 (c) provides that if the action is brought by holders of less than five percent of the shares of any class, (unless the value of the shares exceeds $25,000) the corporate defendant may require the plaintiffs to give security for the costs and reasonable expenses of the action.

This section was given careful consideration by the legislative interim committee and the bar association committee.[153] It was argued that

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[151] § 31-30-20, [24].
[152] § 31-30-21, [45].
[153] Professor Clark's statement to the interim committee provided the basis for amending the section from the way it appeared in House Bill No. 150. He stated:

"I am not clear as to just how this paragraph (b) would operate. It provides that the plaintiffs may be required to pay expenses to the parties named as defendant. In the ordinary derivative suit the corporation is named as a defendant. Does this mean that the parties named as defendant who may receive reimbursement include the corporation and third party defendants, or does it mean only that the plaintiffs must pay expenses to the corporate defendant: or does it apply only where directors or management of the corporation are also named as defendants? It doesn't seem to me that this section spells out with sufficient particularity just how it is to operate.

"Paragraph 'c' of this section is based, I presume, on the New York Statute which has now been in effect for some time. This statute was aimed at preventing the obvious abuses of strike suits by minority shareholders. It has caused a great deal of discussion pro and con in New York and other states. The proponents of sections like this argue that derivative shareholders' actions usually are brought solely for the selfish purpose of the plaintiffs, in the hope that the plaintiffs will be bought off by the management. The resulting settlement is of no benefit to the corporation or the other shareholders, according to the argument. The New York Statute is § 61B, the New York General Corporation Law, which was enacted in 1944 and based on a report made by Mr. Franklin S. Wood, a New York attorney, on behalf of a committee of the New York Chamber of Commerce. This report contained an analysis of nearly 700 shareholder's suits brought in the New York Courts during the decade 1932-1942, and relating to closely held corporations. Mr. Wood also studied nearly 600 suits relating to publicly held corporations. His report indicated that only 8% of the cases resulted subsection (b) was discriminatory as to plaintiffs in that there is no like provision for an "unreasonable defense," and subsection (c) dis-

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in recovery to corporations having publicly held shares and that, even in those successful suits, the recoveries amounted to less than 5% of the amounts asked for in the action.

"Persons opposing this kind of a statute have argued that, although admittedly the shareholder's action may be abused and in fact has been abused, it is the only civil remedy that a stockholder has for breach of fiduciary duty on the part of the directors and the management. For arguments opposing this kind of legislation, see Hornstein, New Aspects of Stockholder's Derivative suits, 47 Colum. L. Rev. 1, 15-20 (1947), and Hornstein, The Death Knell of Stockholder's Derivative Suits in New York, 32 Cal. L. Rev. 123 (1944). It is perfectly clear that only a very small percentage of shareholders in publicly held corporations will be able to meet the requirement imposed by this statute, namely, ownership of 5% of the outstanding shares or ownership of shares having a market value in excess of $25,000. The present New York Statute places this market value figure at $50,000 rather than $25,000. Apparently it is possible for a group of shareholders to combine as plaintiffs and, if their combined holdings exceed the 5% minimum, they cannot be required to post a bond as security for expenses.

"New York Section 61B has been strongly attacked as unconstitutional under the due process clauses of both state and federal constitution. There is a United States Supreme Court case, however, which holds the statute valid under the Federal Constitution. This is Cohen v. Beneficial Industrial Loan Corporation, 337 U.S. 541 (1949). On the whole question of constitutionality, see Zlinkhoff, The American Investor and the Constitutionality of Section 61B of the New York General Corporation Law, 54 Yale L. J., 352 (1945).

"Recognizing that expert opinion differs sharply on the wisdom of these statutes, I would very strongly oppose them for Colorado. Conceding that there may be abuses of the derivative action, this kind of a statute goes far beyond the point necessary to correct the abuses and results in the virtual abolition of the suit, which I would regard as highly undesirable when we already have so few and ineffective ways of controlling management in the interests of the shareholders. I am not aware that there has been any abuse of the shareholders' suit in Colorado."

Professor Clark submitted an additional memorandum on this matter after brief discussion of the section was had by the committees, as follows:

"Due to lack of time at the meeting on September 18 there was not much discussion of Section 43 A imposing a requirement of security upon some shareholders when bringing a derivative action. I should just like to reiterate my very strong conviction that this is an undesirable provision. The evil at which this section is aimed, namely the strike suit, is already cured to some extent in Colorado by Rule 23 (c) of the Rules of Civil Procedure, which provides that a class action shall not be dismissed or compromised without the approval of the court. This rule insures that if the derivative suit is actually brought the court can supervise the compromise so as to make sure that whatever payment is made by the defendants goes to the benefit of the corporation and not just to the plaintiff or his attorney. Furthermore private settlements with plaintiffs bringing strike suits do not benefit such plaintiffs under existing case law in other states, since the rule is that the plaintiff holds the proceeds of the settlement in trust for the corporation. The leading case on this is Clarke vs. Greenberg, 296 New York 146, 71 N.E. 2nd 443 (1946). There is no Colorado case on this to my knowledge but I would suppose that the Colorado courts would follow New York if presented with the problem.

"As I indicated in my original memorandum I do not believe that shareholders' derivative suits have been abused in Colorado and therefore I feel that legislation of this type is a serious mistake. If further corrective legislation is desired however it would seem to me that a statute on the California Model is far preferable to the New York type since it provides that on motion by the defendants the plaintiff can be required to show that there is a reasonable basis for his suit, the plaintiff only being required to deposit security for the defendants' cost in the event that his suit is found by the court to be without reasonable cause. The relevant sections of this California Statute are found in California Corporation Code § 834 (b) & (c) (West 1954)."

criminated against small ownership. It was also pointed out that the right to bring an action for the protection of property is protected by Article II, Section 6 of the Colorado Constitution.[154]

DIRECTORS, OFFICERS, RECORDS AND DIVIDENDS

A. DIRECTORS, BY-LAWS, OFFICERS, BOOKS AND RECORDS

The general management of the corporation is vested in the board of directors "which shall exercise all the powers of the corporation, except as otherwise provided in this act or by its articles of incorporation."[155] This authority can be delegated in part to an executive committee,[156] but the directors are not thereby relieved from liability for those acts for which they are responsible.[157]

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[154] This argument was answered on behalf of the Colorado Bar Association Corporation Committee by Mr. Keith Anderson of Denver, as follows:

"This particular section is designed to regulate derivative suits brought on behalf of corporations by minority shareholders, usually against directors or officers of the corporation. It was designed to prevent the scandalous practices which had arisen in connection with such litigation in several other states, notably New York, and Delaware, and which are probably inevitable sooner or later, in Colorado, unless some legislation of this kind is adopted.

* * *

"Justice Jackson of the United States Supreme Court eloquently summed up the abuses resulting from strike suits in Cohen v. Beneficial Industrial Loan Corp. 337 U.S. 541, 548 (1949) as follows:

" 'Unfortuantely, the remedy itself (stockholder derivative actions) provided opportunity for abuse which was not neglected. Suits sometimes were brought not to redress real wrongs, but to realize upon their nuisance value. They were bought off by secret settlements in which any wrongs to the general body of shareholders were compounded by the suing stockholder, who was mollified by payments from corporate assets. These litigations were aptly characterized in professional slang as "strike suits". And it was said that these suits were more commonly brought by small and irresponsible than by large stockholders, because the former put less to risk and a small interest was more often within the capacity and readiness of management to compromise than a large one.' "

"In these suits corporate funds would be diverted from the corporation to the plaintiff's attorney and there would be no benefit to the corporation even though management may clearly have been at fault.

* * *

"In the American Bar Assocation's Act, which is the basis for S.B. 14, the costs which the plaintiff was required to pay included the fees of the defendant's attorneys. In the judgment of the State Bar Association's Committee on Corporation and Banking, such a provision would have been highly desirable in Colorado. However, it was reluctantly omitted because the Supreme Court of Colorado held in Davidson v. Jennings, 27 Colo. 187 (1900), that requiring the losing party to pay the winning party's attorney fees violated Article II of Section 6 of the Colorado Constitution . . . .

* * *

"Although Section 45 now lacks its sharpest teeth by reason of this deletion we believe that the possibility of being required to pay other expenses may give pause to the typical strike suitor, who commences groundless litigation for purposes of extortion. We further believe that this is accomplished without seriously limiting the rights of legitimate minority shareholders who are actually attempting to correct corporate abuses. No plaintiff who actually believes that he has a meritorious cause of action should object to taking the risk of paying some of the expenses of the defense if he should fail, or to providing a bond or other security for these expenses at the outset of the litigation.

* * *

"To conclude, we should like to urge one practical point which arises not from scholarly study, but from the mundane experience of lawyers in dealing with everyday corporate affairs. As a matter of abstract analysis, the right of a minority shareholder to bring a derivative suit is a great weapon in favor of corporate democracy and a great defense against fraud on the part of management. Whenever a derivative suit is brought and prosecuted in good faith, and actually on behalf of the corporation, it serves these purposes. We believe the possibility of using these actions for such good purposes is preserved by Section 45. On the other hand, the fact which does not appear so readily from academic analysis is that the vast majority of derivative actions have not been brought with any view toward benefitting corporations. They are instead a highly sophisticated and profitable form of extortion. Section 45 has been proposed for the purpose of keeping this valuable tool from being used for the sordid purpose of extortion; we think it does not destroy the tool or prevent its use in any proper manner." Letter from Keith Anderson to David J. Clarke, Feb. 4, 1958.

[155] § 31-31-1, [34].

[156] § 31-31-7, [40].

[157] § 31-31-14, [44].

The section of the new law[158] relating to the number and election of directors is the same as section 34 of the Model Act. It requires a number, not less than three, which shall be fixed by the by-laws, except that the names and the number of the first board of directors must be stated in the articles of incorporation.[159] This permits the organization meeting to be held by the directors[160] since the new law does not require any meeting of the incorporators or of the subscribers.

Section 36 of the new law[161] allows the directors, if the articles of incorporation so provide, to be classified so that only a part of the board is then elected in any one year. This represents a continuation of Colorado law.[162] The Model Act provision restricting classification to boards having nine or more directors is not contained in either the old or the new Colorado corporation law. Since classification of directors makes it impossible in any one year to completely oust the management of a

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[158] § 31-31-2, [35]. Cf. Colo. Rev. Stat. § 31-2-1 (1953) which specifically allows a variable number of directors. Section 31-31-2, [35] appears to allow only a fixed number which can be increased or decreased from time to time by amendment to the by-laws. The restriction in Colo. Rev. Stat. § 31-2-1 (1953) that a decrease within the limits stated in the certificate of incorporation can be made only by stockholders, where the number is variable, points up the possibility under the new section that unless the power of the directors to amend the by-laws is restricted in the articles of incorporation, the directors could, by amendment, frustrate shareholders' cumulative voting rights by reducing the number of directors.

[159] § 31-29-2 (k), [50 (k)].

[160] § 31-29-5, [53].

[161] § 31-31-3. Professor Clark stated to the interim committee:
"Various arguments can be made pro and con on the wisdom of allowing classification. Perhaps the most crucial difficulty is that the classification of directors makes it impossible in any one year to completely oust the management of a corporation and substitute another management. In the leading recent case of Wolfson v. Avery, 126 N.E.2d 701 (Ill. 1955) a classification provision somewhat like this was held invalid in Illinois because it conflicted with the cumulative voting provision, which in Illinois is found in the constitution rather than merely in the statutes. The court said that where directors' terms are classified and staggered in this manner, the cumulative voting privilege is in effect nullified. The reason for this is that when the terms are staggered and only a few of the board of directors is elected in any one year, the percentage of votes required to obtain a representation upon the board of directors is mathematically increased. The effect of this is to cut off the representation which a minority of shares might otherwise be able to achieve. Of course we are not here concerned with any constitutional question, but only with the wisdom of allowing classification. My own view is opposed to classification because it does tend to cut down on minority representation which under modern corporate practice I think is already much too attenuated. The usual argument in favor of classification is that it preserves continuity of management, but I think that that is not ordinarily a problem with the vast majority of corporations, where management tends to perpetuate itself."

[162] Colo. Rev. Stat. § 31-1-6 (5) (1953).

corporation, the inclusion of such a provision in the articles should correspond to the inclusion of a statement allowing or excluding cumulative voting. Consistency appears to require that where classification of directors is included in the articles, a statement should also be included providing that cumulative voting shall not be allowed. The new Colorado law does, however, contain a provision which permits the entire board of directors to be removed, with or without cause, by a vote of a majority of shares entitled to vote for the election of directors.[163] If the number of directors is increased, it is the shareholders who must elect them.[164]

The articles or by-laws must give the board of directors authority to designate an executive committee.[165] Under present Colorado law the board of directors may designate an executive committee by resolution.[166]

With respect to the place and notice of directors' meetings,[167] the new Colorado law permits action by the board without a meeting if all of the directors consent in writing.[168]

Shareholders presently have power to make the by-laws unless the certificate of incorporation authorizes the directors to make them.[169] But under the new law, this power is vested in the directors, including the power to adopt initial by-laws, unless such power is reserved to the shareholders by the articles of incorporation.[170]

The by-laws should list the officers, their time and manner of election, and the authority and duties of each. The officers must consist of a president (who need not be a director, as has been required in Colorado),[171] one or more vice presidents, a treasurer and a secretary. Any two or more offices, except president and secretary, may be held by the same person.[172] There is presently no provision in Colorado relating to the removal of officers. The new law, however, brings the employment of corporate officers within the general principle of agency law that any employee can be fired at any time.[173] The corporation, however, may be sued for breach of contract. This section enables directors to offer some

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163 § 31-31-5 [38].
164 § 31-31-4. [37].
165 § 31-31-7, [40].
166 § Colo. Rev. Stat. § 31-2-1 (1953).
167 § 31-31-8, [41]. Cf. Colo. Rev. Stat. § 31-2-5 (1953)
168 §31-30-22, [139].
169 Colo. Rev. Stat. § 31-1-19 (1953).
170 § 31-31-9, [26]. While the shareholders may have some protection in the fact that by majority vote they can remove the entire board of directors, the section on greater voting requirements (§ 31-30-18, [137]) states that a provision in the articles requiring more than a majority shall control. Hence, it appears that at least one way the legislature might protect shareholders with respect to this vital part of the Act is to except § 31-31-5, [38] from the operation of the section on greater voting requirements.
171 Colo. Rev. Stat. § 31-1-17 (1953).
172 § 31-31-15. [46].
173 § 31-31-16, [47].

security of tenure to attract good executive officers, but also gives them power to discharge, at the risk of incurring liability for damages.

Whether the changes of the new law[174] concerning books and records is an improvement depends upon whether one makes the comparison from the viewpoint of management or of minority shareholders. In general the new law limits the right to inspect books to shareholders of record for six months or to holders of at least five percent of the outstanding shares. However, a court may compel the production of books for examination by any shareholder upon proof of a proper purpose. Present Colorado law allows all shareholders to examine both the books of account and the list of stockholders upon a showing of a proper purpose.[175] The limitation of the new law is aimed at preventing minority shareholders from harassing management with demands to see the books.

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[174] § 31-31-17, [48]. Cf. Colo. Rev. Stat. §§ 31-1-11, 31-2-9, 31-2-10, and 31-2-17. After Sen. Bill No. 14 passed the Senate, the Revisor of Statutes questioned the constitutionality of Section 48, in the following language:

"Subsection (b) of this section is discriminatory as between stockholders both as to period of ownership and as to large and small ownerships. The provision in (e) is merely declaratory of the right to go to court and does not effect discrimination. The question of whether or not this is a valid limitation on a stockholders right can be eliminated by deleting the reference to 5% and by decreasing the six months to a very short period.

"(c) This section already provides for showing a proper purpose for stockholders. This subsection defines an improper purpose, to wit, selling list of stockholders. Would suggest the chances of survival of this section could be strengthened by deleting in line 5 'or any other corporation.' "

"(d) There are some instances in which persons other than shareholders may obtain inspection for some purposes, for example, a judgment creditor with a lien and execution. Would suggest in line 13, page 39, after the word 'shareholders' insert 'or other proper party.' "

Keith Anderson, on behalf of the Bar Association Committee, commented on the Revisor's points, as follows:

"The obvious purpose of this section is to limit the abuses arising when a shareholder buys stock for the sole purpose of obtaining information from the books of the corporation. If the shareholder has a legitimate purpose, he can obtain permission to inspect the corporate books from the court. Every state that has enacted the American Bar Association Model Business Corporation Act has enacted this provision or a very similar one. . . ." Letter from Keith Anderson to David J. Clarke, Feb. 11, 1958.

Professor Clarke advised the interim committee, in part, as follows:

"Paragraph 'd' of this section seems to qualify the restriction in paragraph 'b' by authorizing a court to order inspection of the books, irrespective of the time during which the shareholder has owned his shares and of the number of shares which he owns. This takes away some of the force of the objections to paragraph 'b' but by no means cures those objections because it puts the shareholder to the expense of bringing legal proceedings in order to get a look at the books. This may often be prohibitive, especially where the shareholder owns a small number of shares."

[175] Dines v. Harris, 88 Colo. 22, 291 Pac. 1024 (1930).

Existing law provides that a shareholder owning fifteen percent of the stock may request a detailed statement of the affairs of the corporation.[176] The new law provides that upon written request of any shareholder, the corporation shall mail its most recent annual financial statements showing in reasonable detail its assets and liabilities and the result of its operations.[177]

B. DIVIDENDS

The dividend section of the new law[178] is one of its most important sections. It received extended consideration by the bar association committee and the interim committee. It follows the Model Act through subsection 42 (a). Subsections 42 (c), (e), (f) and (g) are substantially the same as Model Act subsections 42 (c), (d), (e) and the final paragraph, respectively.

It is of particular interest that the Colorado version of subsection 42 (b) does not require that corporations engaged in the business of exploiting natural resources must be given authority in the articles to declare dividends payable from depletion reserves. It does, however, require, along with the Model Act, that each such dividend must be identified as such, and that the amount per share paid from such reserves must be disclosed to the shareholders. It also added a proviso which is not found in the Model Act, to the effect that no such dividend shall be paid which would reduce the remaining net assets of the corporation below the amount to which preferred shareholders are entitled upon liquidation.

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[176] Colo. Rev. Stat. § 31-2-17 (1953).

[177] § 31-31-17 (e), [48 (e)].

[178] § 31-31-10, [42]. Professor Clark stated, with reference to this section:

"Reference should here be made back to Section 2, the definition section, especially the definitions of 'earned surplus' and 'capital surplus'. The present Colorado Dividend provision is Colo. Rev. Stat. § 31-2-12 (1953) which sets up the two tests of insolvency in the equity sense, and impairment of capital, for the validity of a dividend.

"The Model Business Corporation Act, by and large, limits dividends to earned surplus as that phrase is defined. The proposed Colorado statute, however, adds in subparagraph d, the provision that dividends may be paid also out of any net assets in excess of capital, the effect of which is to make available for dividends any capital surplus in addition to earned surplus. This was also done in Virginia in their recent Corporation Code, Va. Code Ann. §§ 13.1-43 (1956). This leaves the Colorado dividend law even broader than it was under the prior statute and instead of using a retained net earnings test for the validity of a dividend, it makes dividends possible if there are retained net earnings or in the alternative, if there is a balance sheet surplus resulting from all kinds of transactions. It is an extremely broad provision. It would allow a dividend, for example, to be paid if the corporation's capital were substantially impaired from any one of a number of reasons provided there were net earnings to cover the dividend. On the other hand, if there were no net earnings but a capital surplus has accrued by reason of unrealized appreciation in the value of the assets, a dividend could be paid. In my view, the statute is seriously deficient as now drawn because it does not protect creditors adequately, nor does it protect the interests of preferred shareholders. . . . See also Hackney, The Financial Provisions of the Model Business Corporation Act, 70 Harv. L. Rev. 1357 (1957).

"The statute as proposed also includes a so-called 'wasting assets' provision allowing a corporation which is in the business of exploiting natural resources to pay dividends out of depletion reserves. In my view and in, I think, the opinion of most conservative accountants, this is undesirable. It means that a mining or oil corporation could pay out substantially all of its capital in dividends without adequate protection for its creditors, or for its preferred shareholders. I will confess, however, that there is such a wasting assets exception in the law of many states such as California and Delaware. This notion that mining corporations should be able to pay dividends without regard to reserves for depletion, arose, I believe, at a time when it was customary for small mining corporations to work one mine and when that was exhausted to go

Subsection 42 (d) of the new law is not found in the Model Act. It allows dividends to be paid out of net assets in excess of the corporation's stated capital:

> ". . . except that no such dividends shall be paid to the holders of any class of shares if such payment would reduce the remaining net assets of the corporation below the total of (1) stated capital, plus (2) additional amounts, not forming part of stated capital, payable in the event of voluntary liquidation to the holders of shares having rights to the assets of the corporation in liquidation preferential to those of the class on which such distribution is made."[179]

In accordance with the definitions of the new act,[180] therefore, dividends may be paid in Colorado out of surplus, subject to the exception quoted above. Hence Colorado's new dividend provisions appear to be as liberal, if not more liberal, than those of any other state which has adopted the Model Act.

The section of the new law relating to distributions in partial liquidation [181] is the same as the Model Act provision. It has no counterpart in present Colorado law. It permits the directors to distribute to shareholders in partial liquidation, out of stated capital or capital surplus, a portion of its assets, cash, or property. However, no such distribution can be made (a) if the corporation is insolvent or would become so, (b) unless the articles so provide or two-thirds of the entire outstanding shares agree, (c) unless all cumulative dividends accrued on preferred or special classes of shares have been fully paid, and (d) if the distribution would reduce the remaining net assets below the aggregate preferential amount payable in event of voluntary liquidation. Each such distribution must be identified as such. This section also authorizes the directors to distribute cumulative preferred dividends out of capital surplus if the corporation has no earned surplus, and is not or would not become insolvent.

The section of the new law relating to the sale, mortgage or lease of assets [182] represents a consolidation of sections 72 and 73 of the Model

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out of business. It seems to me today that most mining corporations and oil companies do not have any intention of doing this, but rather intend to set up reserves for depletion which can then be invested in other mines and other oil wells when the original properties have been exhausted. For companies of this type I would think that the wasting assets exception would not be needed and for companies of the other type such an exception enables them to set up inadequate reserves to protect their creditors." Memorandum of Aug. 14, 1957, to the Interim Committee.

[179] § 31-31-10 (d), [42 (d)].

[180] § 31-27-2 (k), [2 (k)].

[181] § 31-31-11, [43].

[182] § 31-31-12, [75]. Professor Clark stated to the interim committee:

"This section departs in detail from the corresponding section of the Model Business Corporation Act, but it imposes substantially the same rule by requiring a two-thirds vote of the shareholders at a meeting called for the purpose of approving a sale of substantially all the corporate assets not in the usual course of business. The section as drafted here, however, departs in one respect from the Model Act by excluding from the requirement of a two-thirds vote, the mortgage or pledge of substantially all the assets of a corporation not in the ordinary course of business. It is not clear to me why this should be excluded since it would seem that a mortgage or pledge is the kind of extraordinary transaction on which the shareholders should be entitled to vote to the same extent as where the transaction is one of sale, exchange or lease." Memorandum of Aug. 14, 1957, to the Interim Committee.

Act. However, it appears that in the process of consolidating, the Model Act's clear distinction between such transactions made in and outside the regular course of business has been lost. Even where a two-thirds vote of the shareholders is required to effect a sale, exchange or lease of the business, property, assets or franchises of the corporation not in the usual course of business, mortgages and pledges are specifically excepted. The protection provided to shareholders by present Colorado law[183] will be lessened when the new law takes effect.

C. Rights of Dissenting Shareholders

Rights of dissenting shareholders under the new act [184] upon sale, exchange or lease of assets are substantially the same as under the Model Act. The Colorado section, however, was extended to cover leases in addition to sales and exchanges of the business, assets, property or franchises. To preserve their rights shareholders must object in writing prior to the meeting, not vote for the sale, exchange or lease, and within ten days make written demand for the value of their shares as of the day prior to the meeting. After the sale, exchange or lease notice must be given within ten days to dissenting shareholders. If the fair value of the shares is not agreed upon during the succeeding thirty days, dissenting shareholders may petition the court to determine it.

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[183] Colo. Rev. Stat. §§ 31-1-6 (9) and 31-6-2 (1953).

[184] § 31-31-13, [76]. It is noted that the 1957 revisions of the Model Act sections on rights of dissenting shareholders in cases involving mergers and sales of assets (§§ 71 and 74) contained extensive changes which were not considered by the bar association and interim committees.

D. LIABILITY OF DIRECTORS

The section of the new law which relates to liability of directors[185] is the same as the Model Act provision, except that subsection (e) of the Model Act is omitted and subsection (d) was broadened to impose liability on directors who vote for or assent to the making of or guaranteeing of a loan to an officer or director only if the approval of two-thirds of the stockholders was not first obtained.

Under the new law directors who vote for or assent to the declaration of any dividend contrary to the act or the articles of incorporation will be jointly and severally liable to the corporation. However, the amount of liability is limited to the excess over the amount which could have been paid under the act or articles. Consequently, it appears that creditors will have less protection than that which is provided under present Colorado law.[186] The new law also gives directors a right of contribution against either shareholders or other directors. This appears to constitute a change in Colorado law. The liability of shareholders for contribution requires proof that they accepted the dividend with knowledge that it was made in violation of this section of the new law; liability of other directors for contribution requires only proof that they voted for the dividend.[187]

STATED CAPITAL, AMOUNT AND REDUCTIONS, REDEEMABLE SHARES, SURPLUS AND RESERVES

A. STATED CAPITAL

The section of the new law relating to determining the amount of stated capital,[188] makes several changes in present Colorado law.[189] Under the new law stated capital is par for par value shares. Any excess received over par value constitutes capital surplus. The entire consideration received for no par shares constitutes stated capital except that not more than twenty-five per cent of the consideration may be allocated to capital surplus. Allocation, with respect to no par preferred shares is limited to the amount of consideration received in excess of the preference. The board of directors can transfer surplus to stated

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185 § 31-31-14, [44]. Cf. Colo. Rev. Stat. §§ 31-2-12, 31-7-3 and 31-7-15 which, to some extent, cover the subject in piecemeal fashion. Professor Clark advised the interim committee:

"I have no comments with respect to the first three paragraphs of this section. They are taken directly from the Model Act and seem to hold the directors liable on proper grounds. This of course is a change from the existing Colorado Law which holds directors directly liable to creditors for the entire debts of the corporation when they consent to an improper dividend. This is in Colo. Rev. Stat. § 31-2-12 (1953). In this respect the proposed law gives the creditors much less protection than they have under existing law. That may be justified on the ground that the existing statute gives them more than they are entitled to expect."

* * *

"Paragraphs 'f', 'g', 'h' and 'j' of this section seem entirely proper. Paragraphs 'h' and 'i' especially give directors a much needed right of contribution against either shareholders or other directors for their respective shares of illegally declared dividends. Under the present Colorado Statute, I think a director who had been held liable would not have any such right to contribution." Memorandum of Aug. 14, 1957, to the Interim Committee.

186 Colo. Rev. Stat. § 31-2-12 (1953).

187 § 31-31-14, [44].

188 § 31-32-1, [20].

189 Colo. Rev. Stat. § 31-1-15 (1953).

capital in respect of any designated class of shares. The right to allocate a part of the consideration for no par shares to capital surplus may have certain advantages in corporate financing, particularly to provide a source of dividends on preferred shares where no other surplus is available.

B. REDEEMABLE SHARES

The section of the new law which restricts the redemption or purchase of redeemable shares[190] follows the present Colorado law.[191] It prohibits such redemption or purchase when the corporation is or would become insolvent or when such redemption or purchase would reduce the net assets below the amount payable to preferred shareholders. The power to issue shares of preferred or special classes subject to the right of redemption is granted by the new act.[192] Restrictions in this section upon the right to redeem or purchase redeemable shares are in addition to any restrictions that may be in the articles.[193] The act does not require that the purchase or redemption of redeemable shares be out of earned surplus or that it be subject to the approval of two-thirds of the shares if the source is capital surplus.[194] Shares reacquired, other than redeem-

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[190] § 31-32-2, [62].
[191] Colo. Rev. Stat. §§ 31-3-6 and 31-1-25 (1953).
[192] § 31-30-1, [14].
[193] Ibid.
[194] § 31-28-2 (4), [5 (4)].

able shares, may be cancelled by action of the board of directors.[195] Stated capital may otherwise be reduced pursuant to section 66[196] of the new law and subject to the rights of a class of shares to vote as a class where the reduction of stated capital affects the rights of the class.[197]

Under the new act, when redeemable shares are purchased or redeemed, they are cancelled and a statement of cancellation must be filed with the Secretary of State. Then they are restored to the status of authorized but unissued shares, unless the articles provide that such shares shall not be reissued. In that event the filing of the statement constitutes an amendment to the articles and reduces the number of authorized shares by the number of shares cancelled.[198] A corporation, by resolution of its board of directors, can also cancel shares reacquired by it, other than redeemable shares.[199]

C. REDUCTION OF STATED CAPITAL

The section of the new law[200] relating to the reduction of stated capital where an amendment to the articles is not required and a cancellation of shares is not involved, is applicable to nothing more than a reduction of the stated capital represented by issued no par shares or, in the case of par value shares, where the stated capital has been increased above par value and a reduction of stated capital to not less than par value is desired. The procedure requires that the matter be submitted to the shareholders and, if it is approved by majority vote, a statement must be filed with the Secretary of State. Preferred shareholders are protected by a special provision at the end of the section.

D. SURPLUS AND RESERVES

The new law provides that any surplus created by a reduction of stated capital shall be capital surplus.[201] It also provides that earned surplus can be transferred to capital surplus.[202] Capital surplus can be applied to reduce or eliminate any deficit arising from losses but only after first eliminating the earned surplus and only to the extent that losses exceed earned surplus. If a reserve is created out of earned surplus the amount reserved is not available for the payment of dividends or other distributions except as expressly permitted by the act.[203]

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[195] § 31-32-5, [65].
[196] § 31-32-6.
[197] § 31-29-8, [56].
[198] § 31-32-3, [63].
[199] § 31-32-4, [64].
[200] § 31-32-5, [65].
[201] § 31-32-6, [66]. Professor Clark wrote to the interim committee:
"The section as drawn provides that such a capital surplus may be used only for certain purposes. This limitation on the use of capital surplus, however, is rather superfluous in view of the changes made in Section 42 in this proposed Code. As drafted in the Model Business Corporation Act, dividends can be paid primarily only out of earned surplus, and this section of the Model Act reinforces that by making capital surplus available only for limited purposes. But once the payment of dividends is allowed out of capital surplus it doesn't make much sense to say in this section that the corporation may use capital surplus for the reduction of deficits, but only after first eliminating the earned surplus. In other words, section 42 and this section should be read together to some extent and the drafting of this section no doubt should be changed to accord with the changes made in section 42. See the discussion of this section in Hackney, The Financial Provisions of the Model Business Corporation Act, 70 Harv. L. Rev. 1357, 1386 (1957)". Memorandum of Aug. 14, 1957, to the Interim Committee.
[202] § 31-32-6, [66].
[203] § 31-31-10 (b), [42 (b)]

MERGER OR CONSOLIDATION

Two or more domestic corporations, under the new law,[204] may merge into one corporation or may consolidate into a new corporation. Plans of merger or consolidation must be adopted by resolution of the board and must contain the names of the corporations proposing to merge or consolidate, the name of the surviving corporation (in the case of mergers) or the name of the new corporation (in the case of consolidations), the terms and conditions of the proposed merger or consolidation, and the manner and basis of converting the shares of the merging and consolidating corporations into the shares of the surviving or new corporation. In the case of mergers, a statement of any changes in the articles of the surviving corporation, and, in the case of consolidations, all of the statements required to be set forth in original articles of incorporation must be set forth in the plans.

Each board of directors is required to present the plan or a summary of it to shareholders at either an annual or special meeting. A two-thirds assent of all outstanding stock is required. Each outstanding share is entitled to vote, whether or not such share has voting rights under the articles. If any class of shares is entitled to vote as a class, the plan must be approved by a two-thirds vote of that class *and* a two-thirds vote of the total outstanding shares. However, a class of shares is entitled to vote as a class only when the plan of merger or consolidation contains a provision which, if contained in a proposed amendment to the articles of incorporation, would entitle such class of shares to vote as a class.[205]

The two-thirds requirement in the new law represents a welcome clarification of the present conflict in Colorado statutes. Presently section 31-4-1 requires a three-fourths vote of shareholders for consolidation, whereas section 31-4-6 requires only two-thirds.

The new law provides that even after shareholder approval is obtained, the merger or consolidation may be abandoned pursuant to

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[204] §§ 31-33-1, [67] and 31-33-2, [68].
[205] § 31-29-8, [56].

provisions for abandonment set forth in the plan. Such action must be taken, however, prior to the filing of articles of merger or consolidation. After the filing of such articles, the merger or consolidation becomes effective upon issuance of a certificate of merger or consolidation by the Secretary of State.[206] The publication requirement of the present law[207] has been eliminated as has the requirement that certified copies of merger or consolidation papers must be filed with the county clerk.[208] In addition, the present prohibition against consolidation by certain railroad and telegraph companies[209] is not contained in the new law.

The section of the new law pertaining to the effect of merger or consolidation[210] follows the Model Act and appears to clarify present Colorado law[211] without substantial change.

The new law permits the merger of a subsidiary corporation without approval of the shareholders if the surviving corporation owns at least ninety-five per cent of each class of the outstanding shares of the subsidiary.[212] A copy of the plan of merger must be mailed to each shareholder, however, and the articles of merger cannot be delivered to the

[206] § 31-33-5, [72].
[207] Colo. Rev. Stat. §§ 31-4-2, 31-4-1 and 31-4-5 (1953).
[208] Id. §§ 31-4-1, 31-4-5.
[209] Id. § 31-4-4.
[210] § 31-33-5, [72].
[211] Colo. Rev. Stat. §§ 31-4-8 and 31-4-10 (1953).
[212] § 31-33-6, [71].

Secretary of State until thirty or more days after such mailing. Such delay is for the protection of dissenting shareholders.[213]

Under present Colorado law[214] a dissenting shareholder must make written demand for payment of the value of his shares within twenty days after the filing of the agreement of merger or consolidation. Such value then is determined as of the effective date of the merger or consolidation, omitting any element of value arising from the merger or consolidation. If an agreement on value is not reached within thirty days the value is determined by appraisers appointed by the parties or by a court. The new law appears to be more workable. Under the new law[215] a shareholder must file written objections with the corporation prior to or at the meeting of shareholders and must not vote in favor of the merger or consolidation. Within ten days after the meeting he must make written demand for payment of the fair value of his shares as of the day prior to the meeting. If an agreement is not reached within thirty days after the effective date of merger or consolidation, then the shareholder must, within sixty days, petition the court to determine the fair value.

If domestic and foreign corporations are merged or consolidated, the new law provides that each corporation will be governed by the laws of the state under which it is organized.[216] If the surviving or new corporation is to be governed by the laws of another state, it must qualify as a foreign corporation in order to do business in Colorado. It must also file with the Secretary of State: (1) an agreement to accept process in Colorado in any proceeding to enforce an obligation of or the rights of a dissenting shareholder of the former domestic corporation, (2) an irrevocable appointment of the Secretary of State to accept service of process, and (3) an agreement to pay dissenting shareholders the amount to which they are entitled under this act. The effect of the merger or consolidation of domestic and foreign corporations is the same as in the case of merger or consolidation of domestic corporations if the surviving or new corporation is to be governed by the laws of Colorado. If the surviving or new corporation is to be governed by the laws of another state, however, the effect is the same as in the case of domestic corporations except to the extent that the laws of the other state provide otherwise.

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[213] § 31-33-8, [74].
[214] § 31-4-9.
[215] § 31-33-8, [74]. The 1957 revisions to the Model Act contained a revision of this section which was not considered by the Legislative Interim Committee.
[216] § 31-33-7, [73].

DISSOLUTION—VOLUNTARY AND INVOLUNTARY

A. VOLUNTARY DISSOLUTION

The new law, following the Model Act, provides five methods for dissolving a corporation, exclusive of the expiration of its period of existence: (1) by its incorporators within three years after incorporation if it has not commenced business and has not issued any shares,[217] (2) by consent of the shareholders,[218] (3) by voluntary act of the corporation,[219] (4) by suit filed by the Attorney General,[220] or (5) by an action of a shareholder.[221]

Voluntary dissolution by consent of the shareholders requires unanimous written consent. Voluntary dissolution by act of the corporation requires approval of at least two-thirds of all outstanding shares in addition to a two-thirds class vote where required.[222] When the written consent of all shareholders is obtained, or upon adoption of a resolution by vote of the shareholders a statement of intent to dissolve must be filed,[223] after such statement is filed the corporation must notify its creditors and proceed to liquidate its business and affairs.[224] The new law disposes of the possibility of a multitude of creditors' suits or suits by dissatisfied shareholders, by authorizing the corporation to apply to the district court to have the liquidation continued under the supervision of the court.[225] Upon filing the statement of intent to dissolve,

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[217] § 31-34-1, [77]. This is the same as the Model Act, except that the Model Act permits dissolution within two years. Provision for dissolution under similar circumstances was provided for in Colorado law for many years [Colo. Rev. Stat. § 31-6-3 (1953)], but such section was amended in 1955 (SL 1955, 232) [Id. § 31-6-3 (Supp. 1957)] and the amendment did not continue the provision for dissolution under such circumstances by action of a majority of the incorporators or directors, but provided for dissolution only upon vote of two-thirds of the outstanding stock.

[218] § 31-34-2, [78].

[219] § 31-34-3, [79].

[220] § 31-34-13, [90].

[221] § 31-34-13, [90].

[222] §§ 31-34-2, [78]; 31-34-3, [79].

[223] § 31-34-4, [80].

[224] § 31-34-5, [82].

[225] See § 31-31-14, [44] for liability of directors who vote for a distribution of assets to shareholders during liquidation without paying or providing for payment of creditors.

the corporation must cease to carry on its business, except as necessary for winding it up but its corporate existence continues until issuance of a certificate of dissolution or a decree dissolving the corporation.[226]

After the corporation's business has been liquidated, the officers must execute articles of dissolution setting forth, *inter alia,* that a statement of intent to dissolve has been filed, that all debts have been paid, that the remaining property has been distributed to shareholders, and that there are no suits or criminal proceedings pending against it.[227]

Upon delivery of the articles of dissolution to the Secretary of State, a certificate of dissolution is issued and the existence of the corporation ceases "except for the purpose of suits, other proceedings and appropriate corporate action by shareholders, directors and officers as provided in this act."[228]

The new law contains several provisions for revoking voluntary dissolution proceedings prior to the issuance of the certificate of dissolution.[229] This is done by written consent of all of the shareholders or by the corporation upon vote of at least two-thirds of all outstanding shares. Upon filing a statement of revocation the corporation may again carry on its business.

B. Involuntary Dissolution

1. *By the State*

The new law authorizes the Secretary of State, commencing five years after January 1, 1959, to certify to the Attorney General the name of any corporation which has been defunct for five years, or has procured its articles of incorporation through fraud, or has continued to exceed or abuse the authority conferred upon it by law, or has failed for thirty days to maintain a registered agent in Colorado, or has failed for thirty days to file a statement of change of its registered office or registered agent.[230] A notice of such certification must be mailed to the corporation which then has thirty days in which to remove or remedy the cause for certification. After that period the Attorney General is required to file an action to dissolve the corporation. If, after the action is filed, the corporation removes or remedies the cause and pays the cost of the action plus a penalty of fifty dollars, the action for dissolution abates.[231] The new law contains special provisions concerning venue and process with respect to such actions commenced by the Attorney General.

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226 § 31-34-6, [81].
227 § 31-34-7, [87].
228 §§ 31-34-8, [88]; 31-34-23,[100]. Note also that a certificate of dissolution can be based upon articles of dissolution which merely state that adequate provision has been made for the payment of creditors, for example.
229 §§ 31-34-9, [83]; 31-34-10, [84]; 31-34-11, [85]; 31-34-12, [86].
230 § 31-34-13, [90].
231 § 31-34-14, [91].

2. *By a Shareholder*

The new law authorizes the district courts, upon suit by a shareholder, to liquidate the assets and business of a corporation when it is established either (1) that the directors are deadlocked, the shareholders are unable to break the deadlock, and that irreparable injury to the corporation is being suffered or threatened, *or* (2) that the shareholders are deadlocked, have failed for two consecutive annual meeting dates to elect successors to directors, and that injury to the corporation or a shareholder is being suffered or threatened.[233] Both subsections follow the Model Act except that injury to the corporation or a shareholder was added to the deadlocked shareholders situation. The new law, in so far as it requires that injury be established in either case, appears to continue the case law of Colorado that courts will not liquidate the assets of a going corporation merely because the directors or shareholders are deadlocked.[234]

The provision of the new law relating to the procedure in case of liquidation by a court[235] is more orderly and explicit than the present law.[236] It deals specifically with the duties of a liquidating receiver and allows compensation to be paid to receivers and to attorneys in the proceeding out of the assets of the corporation; it also give the court exclusive jurisdiction of the corporation and its property, wherever situated. The court may require all creditors to file proofs of claims by a certain date at the risk of being barred from participating in the distribution of the corporation's assets.[237] Assets distributable to a creditor or shareholder who is unknown or cannot be found must be deposited with the State Treasurer who must pay them over to a proper claimant.[238]

The new law contains a section[239] taken from present Colorado law[240] which is not found in the Model Act. It vests the title to corporate

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[232] § 31-34-15, [92].
[233] § 31-34-13, [90].
[234] Savageau v. J.&R.A. Savageau, Inc., 132 Colo. 75, 285 P.2d 810 (1955); Hepner v. Miller, 130 Colo. 243, 274 P.2d 818 (1954); Eureka Coal Co. v. McGowan, 72 Colo. 402, 212 Pac. 521 (1922).
[235] § 31-34-16, [93].
[236] Colo. Rev. Stat. § 31-6-8 (1953).
[237] § 31-34-20, [95].
[238] § 31-34-24, [99].
[239] § 31-34-22, [145].
[240] Colo. Rev. Stat. § 31-6-5 (1953).

property, upon dissolution, in the trustees, directors, or managers. It authorizes them to sue for the recovery of property or debts due the corporation, or for damage done to the property. It further authorizes the trustees,[241] to "hold, sell and dispose of any such property, to divide the residue of the moneys received . . . among the shareholders . . . in proportion to the amount paid upon stock of each shareholder."[242] The trustees are jointly and severally liable for property coming into their hands.

The new law also contains a section following the Model Act, which provides a two year limitation period on suits by or against the corporation after the date of dissolution.[243]

FOREIGN CORPORATIONS

To a very large extent the Colorado Corporation Act adopted the provisions of the Model Act which relate to foreign corporations. The section of the Colorado act relating to the admission of foreign corporations,[244] made two changes: (1) it specifically prohibited a foreign banking or insurance corporation from procuring a certificate of authority to transact business in this state under the provisions of the act, and

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[241] It is noted that the language from which this section was taken [Colo. Rev. Stat. § 31-6-5 (1953)] formerly followed Colo. Rev. Stat. § 31-6-1 (1953), by which the board of directors or trustee, or managers, by whatever name known, acting last before the time of dissolution, and the survivors of them, were made trustees of the creditors and stockholders. Hence, it appears that the term "trustees" was intended to include trustees, directors, managers, or their survivors, acting as trustees.

[242] This is not entirely clear. The only reasonable interpretation is that it means in proportion to the amount paid to each shareholder upon stock of each shareholder as in a prior distribution.

[243] § 31-34-23, [100]. Cf. Colo. Rev. Stat. § 31-6-7 (1953).

[244] § 31-35-1, [101]. Professor Clark advised the interim committee:

"It seems to me that the list of activities included in this section, which expressly do not amount to transacting business within Colorado, is too broad and places some handicaps in the way of Colorado creditors who may wish to recover from foreign corporations. The comment to this section in the Model Act states that this list of activities reflects the opinions of courts which have passed on the question of what is doing business. I would take issue with that statement, at least so far as the Colorado cases are concerned. It is true that certain of the activities in this list have been held not to amount to transacting business within the state, but only where the activities have been single, isolated transactions. For example, the case of Miller v. Williams, 27 Colo. 34 (1899), held that a single act of acquiring negotiable securities secured by a trust deed on Colorado real estate would not amount to doing business in the state; and Kephart v. People, 28 Colo. 73 (1900) held that a suit brought in Colorado by a foreign corporation to collect a Colorado State warrant, is not doing business in Colorado. But the Court again emphasized that this was a single transaction, not a connected series of transactions. To the same effect is Roseberry v. Valley Building and Loan Association, 35 Colo. 132 (1905). With a special reference to paragraph "f", I would cite the case of Union Mutual Life Insurance Company v. District Court, 97 Colo. 108 (1935), which held that where a foreign life insurance company advertised over a Colorado radio station under an agreement by which the radio station received and forwarded to the insurance company inquiries about policies, the insurance company was doing business in the state, even though the policy did not become effective until issued by the Company at its home office. This case goes quite a long way in extending the concept of doing business within the jurisdiction and it would certainly be overruled by the proposed Section 99. The leading case in the United States on this whole problem is International Shoe Company v. Washington, 326 U.S. 310 (1945), which makes the concept of doing business turn on continuous activities within the state, no matter how slight they may be. This concept of continuing activities is not referred to at all in the proposed statute. The statute as written would seem to mean that even if the foreign corporation customarily and continuously solicited orders, for example, by mail, that would not be considered to be doing business within the state, nor would it where the foreign corporation made a regular practice of creating evidences of debt and taking mortgages on Colorado property. I think this is an important matter because the statute as drawn would place upon Colorado creditors the burden of going into some other state in order to sue foreign corporations upon a claim which really arose in Colorado. It seems to me that the burden and

(2) it omitted the list of activities contained in the Model Act which would not constitute transacting business. This omission leaves the question of what constitutes doing business in Colorado to the courts.[245]

Failure to obtain a certificate of authority deprives a foreign corporation of the right to maintain an action in Colorado until such a certificate has been obtained. It also subjects a foreign corporation to a penalty of ten dollars per year, plus all fees and franchise taxes which would have been imposed had it received a certificate.[246]

A foreign corporation which has qualified to do business is entitled to the same rights and privileges as a domestic corporation. The effect

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expense of such a lawsuit is unjustified where it arose out of a continued course of action within Colorado. I would, therefore, suggest, at the least, the addition of a phrase in this section indicating that continuous activities in the state, even though they are of a kind falling within one of the listed transactions, ought to subject the foreign corporation to service of process within Colorado." Memorandum of Aug. 14, 1957, to the Interim Committee.

When the Bar Association Committee and the Interim Committee considered this section and were unable to decide whether or not to retain any of the list of activities, Professor Clark agreed to determine to what extent the Model Act list was followed by other states which have used the Model Act as a guide. He thereafter advised:

"I have checked the statutes of the five states which have recently revised their corporation laws by substantially adopting the Model Act. Of the five, two, Texas and Oregon, have enacted section 99. Tex. Bus. Corp. Act. art. 8.01 (1956); Ore. Rev. Stat. § 57.655 (1955). The other three, Virginia, Wisconsin and the District of Columbia, have left out that part of section 99 which lists activities not to be deemed transacting business, Va. Code Ann. § 13.1-102 (1956); Wis. Stat. § 180.801 (1955); D.C. Code Ann. § 29-933 (1956 Supp.). I should correct myself as to Wisconsin: They did include some activities not to be considered doing business, but they are not the ones to which I would take exception, since they were (a) holding directors' meetings, (b) maintaining bank accounts, (c) maintaining offices for the sale or exchange of securities, (d) soliciting orders for acceptance outside the state, and (e) creating evidences of debt or mortgages on property located outside the state.

"It seems to me that the trouble with section 99 is that it purports to exclude the named acts from the concept of doing business for all purposes under the corporation law. The cases dealing with 'doing business' have often said that the meaning of the concept varies with the question involved in the case. Thus a corporation may be held to be doing business for the purpose of being sued in the state, but not for the purpose of being subject to certain penalties or taxes. So far as doing business for the purpose of being sued within the state is concerned, the cases have been moving in the direction of broadening that concept, whereas section 99 would narrow it. The recent LeTourneau case only illustrates that Colorado is out of line with the authorities in other jurisdictions in this respect. In other words, it seems to me that section 99 has the defect of lumping all problems of 'doing business' in one rule, and that rule is much too prejudicial to Colorado citizens." Letter from Homer H. Clark to Robert D. Charlton, Nov. 12, 1957.

[245] § 31-35-1, [101].

[246] §§ 31-35-3, [119]; 31-36-11, [129].

of this is to prohibit it from transacting in Colorado any business which a domestic corporation could not transact.[247]

If a foreign corporation changes its name to one already preempted in Colorado,[248] it may transact business in Colorado under the old name for 180 days during which it is required to change its name in Colorado to one which is available.[249] The filing of an amendment to the articles changing the corporate name does not thereby authorize the corporation to transact business under any other name than that set forth in its certificate of authority.[250] Any change in name requires the foreign corporation to procure an amended certificate of authority.[251]

A foreign corporation must file with the Secretary of State an application for a certificate of authority, on forms prescribed by the Secretary of State.[252] The fee is sixty dollars.[253] Upon delivering duplicate originals of the application to the Secretary of State, together with a copy of its articles of incorporation and all amendments thereto,[254] the Secre-

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[247] § 31-35-4, [102].
[248] §§ 31-35-5, [103]; 31-35-11, [113].
[249] § 31-35-6, [104].
[250] § 31-35-10, [111].
[251] § 31-35-11, [113].
[252] § 31-35-7, [105].
[253] § 31-36-4, [123]. The amount of such fee was determined on the basis of the fees charged to Colorado corporations by other states.
[254] § 31-35-8, [106].

tary of State is authorized to issue a certificate of authority,[255] and, upon such issuance, the corporation can transact business, subject to the right of the state to suspend or to revoke its authority as provided in the act.[256] A copy of any amendment to the articles of incorporation of a foreign corporation must be filed with the Secretary of State.[257]

A foreign corporation may withdraw from this state by procuring from the Secretary of State a certificate of withdrawal.[258]

The new law contains a section authorizing service of process on the Secretary of State if a foreign corporation fails to appoint or maintain a registered agent, or whenever such agent cannot be found at the registered office, or whenever the certificate of authority is suspended or revoked.[259]

The requirement that foreign corporations shall have a registered agent and a registered office in Colorado is discussed above.[260]

REPORTS, FEES, FRANCHISE TAXES, PENALTIES

A. REPORTS

The annual report, as under present law, must be filed between January 1st and May 1st of each year.[261] If it fails to conform to the requirements of the new law, the corporation has until August 1st to amend before the penalties prescribed for failure to file become applicable.[262]

B. FEES

For filing articles of incorporation the following fees will be charged:[263]

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255 § 31-35-9, [107].
256 § 31-35-12, [116].
257 § 31-35-10, [111].
258 § 31-35-15, [114].
259 § 31-39-19, [110].
260 See text at note 81, supra.
261 § 31-36-1, [120]. Cf. Colo. Rev. Stat. § 31-7-11 (Supp. 1957).
262 § 31-36-2, [121].
263 § 31-36-4, [123].

Authorized Capital Stock	*Fee*
Less than $50,000:	$ 25.00
$50,000 or more but less than $150,000:	40.00
$150,000 or more but less than $250,000:	55.00
$250,000 or more but less than $500,000:	85.00
$500,000 or more but less than $1,000,000:	165.00
$1,000,000:	165.00
For each $1,000 over $1,000,000:	.20

C. FRANCHISE TAXES

A franchise tax for each calendar year will be charged each domestic and foreign corporation at the following rates:[264]

Authorized Capital Stock	*Franchise Tax*
Less than $50,000:	$ 10.00
$50,000 or more but less than $100,000:	20.00
$100,000 or more but less than $250,000:	40.00
$250,000 or more but less than $500,000:	65.00
$500,000 or more but less than $1,000,000:	100.00
$1,000,000 or more:	250.00

The franchise tax for part of a year is pro-rated at the rate of one-tenth of the tax for each month between the issuance of the certificate of incorporation or certificate of authority and January 1st of the succeeding calendar year.

In determining both filing fees and franchise taxes, no par shares are to be valued at one dollar per share.[265]

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[264] §§ 31-36-6, [125] and 31-36-7, [126]. The annual franchise tax system was favored by the interim committee as a means to end the senseless method by which corporations have been taxed in the past. Such method was roundly criticized in a series of articles published in The Denver Post, Feb. 8-12, 1955. The schedules of the franchise tax system and filing fees in the new law were intended to permit the creation of small corporations at a minimum cost and still maintain the same level of revenue to the State from the corporation tax as in the past.

[265] § 31-36-8, [127].

D. PENALTIES

The franchise tax is payable at the time the annual report is filed. If such tax is not paid before December 31st of the year in which it becomes due, the Secretary of State is required to give written notice to the corporation by May 1st of the following year.[266] If the corporation then fails to pay the tax it becomes subject to a penalty of ten dollars.[267] If it fails for two consecutive years to pay the tax, the Secretary of State is required to give written notice to the corporation and by publication. Upon proof of publication being filed, the corporation shall be deemed defunct and no longer competent to transact business in Colorado. However, shareholders may hold meetings for the election of directors, and the corporation may continue to hold, mortgage, sell or convey real estate, make any required reports, and elect corporate officers.

Any defunct corporation may become reinstated by filing all reports and paying all taxes, fees and penalties.[268]

CONCLUSION

The new Colorado Corporation Act unquestionably constitutes a marked improvement over prior law. It not only fills gaps in prior law, but also clarifies many confused areas. Moreover, the law has been rendered more accessible and more usable by generally following the Model Act's logical scheme of arrangement.

While problems of construction undoubtedly will arise, the Colorado courts in the future may look to a growing body of case law from other states which have used the Model Act as a guide. Further assistance to the courts and to Colorado attorneys will be found in the annotations to the Model Act now being prepared by the American Bar Association.[269]

It will be understood, of course, that the new act does not provide solutions for all future, or even present, problems of corporation law. Revisions to the Model Act from time to time by the A.B.A. committee may be expected, and those revisions should be carefully studied for possible adoption in Colorado. In addition, it is hoped that Colorado attorneys will recommend to the legislature such amendments to the new act as will represent further improvements in our Corporation Law.

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[266] § 31-36-10, [128].
[267] § 31-36-11, [129].
[268] § 31-36-9, [89].
[269] Such annotations will be published in The Business Lawyer.

APPENDIX

TABLE OF COMPARATIVE SECTION NUMBERS

(Where corresponding sections of the Colorado Corporation Act and the Model Business Corporation Act are identical, an asterisk has been placed after the prospective Colo. Rev. Stat. section number. If, in the author's opinion, they are substantially the same, such section numbers are followed by two asterisks. Unless otherwise indicated, Model Act Section numbers refer to the 1953 Revision of such Act.)

Prospective Colo. Rev. Stat. Nos.	SL 1958 Ch. 32, S. Nos.	Model Business Corp. Act S. Nos.
APPLICATION AND DEFINITIONS		
31-27-1	1	1
31-27-2	2	2
31-27-3	3	3
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31-27-5*	142	141
31-27-6*	144	143
31-27-7	149	...
31-27-8	143	142
CORPORATE POWERS AND LIMITATIONS		
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31-28-2	5	5
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31-28-4	140	139
31-28-5*	6	6
31-28-6	7	7
31-28-7*	8	8
31-28-8	9	9
31-28-9*	10	10
31-28-10*	11	11
31-28-11**	12	12
31-28-12	13	13
31-28-13	131	130
31-28-14*	132	131
31-28-15*	133	132
31-28-16*	134	133
31-28-17*	135	134
31-28-18*	136	135
ARTICLES OF INCORPORATION AND AMENDMENTS		
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31-29-3	51	49
31-29-4*	52	50
31-29-5*	53	52
31-29-6	54	53
31-29-7	55	54
31-29-8*	56	55
31-29-9*	57	56
31-29-10*	58	57
31-29-11*	59	58
31-29-12	60	59
31-29-13**	61	59A (1955)
SHAREHOLDERS AND SHARES OF STOCK		
31-30-1*	14	14
31-30-2	15	15
31-30-3*	16	16
31-30-4	17	17
31-30-5	18	18
31-30-6	19	18A (1955)
31-30-7*	21	20
31-30-8*	22	21
31-39-9*	23	22
31-30-10	25	24
31-30-11*	27	26
31-30-12**	28	27
31-30-13*	29	28
31-30-14	30	29
31-30-15*	31	30
31-30-16	32	31
31-30-17	33	32
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31-30-19**	138	137
31-30-20	24	23
31-30-21	45	43A (1955)
31-30-22	139	138
DIRECTORS, OFFICERS, RECORDS, DIVIDENDS		
31-31-1	34	33
31-31-2*	35	34
31-31-3	36	35
31-31-4*	37	36
31-31-5	38	36A (1955)
31-31-6*	39	37
31-31-7*	40	38
31-31-8*	41	39
31-31-9*	26	25
31-31-10	42	40
31-31-11*	43	41
31-31-12	75	72, 73
31-31-13	76	74
31-31-14	44	43
31-31-15*	46	44
31-31-16*	47	45
31-31-17**	48	46
STATED CAPITAL, AMOUNT AND REDUCTION, REDEEMABLE SHARES, SURPLUS AND RESERVES		
31-32-1*	20	19
31-32-2*	62	60
31-32-3	63	61
31-32-4*	64	62
31-32-5*	65	63
31-32-6*	66	64

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Prospective Colo. Rev. Stat. Nos.	SL 1958 Ch. 32, S. Nos.	Model Business Corp. Act S. Nos.
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31-33-2*	68	66
31-33-3	69	67
31-33-4*	70	68
31-33-5**	72	69
31-33-6**	71	68A (1955)
31-33-7*	73	70
31-33-8	74	71

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31-34-2	78	76
31-34-3*	79	77
31-34-4*	80	78
31-34-5	82	80
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31-34-7	87	85
31-34-8*	88	86
31-34-9*	83	81
31-34-10*	84	82
31-34-11*	85	83
31-34-12*	86	84
31-34-13	90	87, 90
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31-34-15	92	89
31-34-16	93	91
31-34-17*	94	92
31-34-18	97	95
31-34-19*	98	96
31-34-20	95	93
31-34-21*	96	94
31-34-22	145	....
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31-35-3**	119	117
31-35-4*	102	100
31-35-5	103	101
31-35-6	104	102
31-35-7	105	103
31-35-8**	106	104
31-35-9*	107	105
31-35-10*	111	109
31-35-11*	113	111
31-35-12	116	114
31-35-13*	117	115
31-35-14*	112	110
31-35-15*	114	112
31-35-16*	115	113
31-35-17*	108	106
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31-36-3	122	120
31-36-4	123	121
31-36-5	124	122
31-36-6	125	125
31-36-7	126	126
31-36-8	127	....
31-36-9	89	86A (1955)
31-36-10	128	127
31-36-11	129	128
31-36-12*	130	129